Quarterly 2/2000

POLISH ECONOMIC OUTLOOK
TRENDS • ANALYSES • FORECASTS

Summary

In 1Q00, the Polish economic situation deteriorated. We estimate that economic growth was slightly lower than that in 4Q99: GDP and domestic demand grew 6.0% and 6.6% yoy respectively. The growth rate of domestic consumption demand was lower and that of investment demand higher than in previous quarter. At the same time, the contribution of stockbuilding in GDP growth was significant. The resumption of an upward trend in domestic demand (in 4Q99 its growth was slower than that of GDP) occurred at the expense of a deterioration in the current account balance which reached a record high of 9.5% of GDP. Foreign demand for Polish-made products weakened, mainly because of the weak euro, the relatively strong zloty and lack of adjustment of the Polish industry's structure to the demand in EU countries.

Favourable trends in the Polish economy include higher economic efficiency, reflected in a double-digit increase in labour productivity in industry and in lower unit labour costs. The continuation of this trend may lead to higher levels of corporate savings, improve their competitive edge, as well as increase exports and investment demand.

Another worrisome trend observed in 1Q00 was a rise in unemployment, whose rate increased more than what should have resulted from the seasonal drop in labour demand. Its level (13.9% by end-March 2000) reached the record high since mid-1996. In addition, inflation also registered an increase. In 1Q00, CPI rose 10.3% yoy. In our opinion, this was caused mainly by supply constraints, high crude oil prices in world markets and a rise in PPI.

We expect continued growth of the Polish economy: GDP is likely to increase 5.4% and 6.3% in 2000 and 2001 respectively. This gain is economically feasible despite a much tighter economic policy in 2000 and the trend towards balanced economic growth. As a result, in 2000 and 2001 domestic demand growth may be relatively low, amounting to 5.2% and 6.8% respectively.

We expect a gradual decline in inflationary pressures after July 2000. We also anticipate that until that time the inflation rate will hover around 10%. In the next few months inflation may fall reaching 7.3% in December. The average price rises are expected to be 9.5% and 6.2% in 2000 and 2001 respectively.

In our opinion, the current account balance is likely to improve. However, the fundamental precondition for this is that the trend towards the appreciation of the zloty (by making use of a special government's foreign currency account with the NBP) is arrested and exports increased. Higher demand in EU countries may positively affect Poland's balance of payments. On the other hand, the weak euro may effectively dampen Polish exports. We forecast the current account deficit to reach US$12.7 billion (7.4% of GDP) and US$12.9 billion (6.7% GDP) in 2000 and 2001 respectively. In contrast to 1999, the inflow of foreign capital to Poland will more than offset the current account deficit, and increase the official foreign currency reserves from the forecasted value of US$27.6 billion by end-2000 to US$27.9 billion by end-2001.

The fifth issue of Polish Economic Outlook (PEO) analyses the economic situation in Poland in 1Q00 and the trends observed throughout the entire previous year. Primary short- and long-term threats as well as the most recent economic outlook over the period 2000–2001 are provided. Particular attention is drawn to the most serious threat to the Polish economy – the high deficit on the current account as well as the low probability of reaching the inflation target for this year. This issue's special topic is devoted to changes in the structure of the Polish balance of payments in view of the process of accession to the European Union.

In future issues of PEO a risk index of financial crisis in Poland and an inflation rate computed according to the EU nomenclature (i.e. HICP) will be included.

All estimates and forecasts are derived from data available until end-April 2000. One should note that various data for previous years are updated in line with changes in official statistics.

We kindly remind our readers that the PEO is available in hard copy as well as in PDF file format – both in English and Polish.

For information about subscription please contact Michał Górzyński (pgtop@case.com.pl) or check our web site (www.case.com.pl).

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Assessment of the economic situation in 1Q00

The Polish economic situation in 1Q00 deteriorated compared to end-1999. Despite the relatively high growth of GDP and considerable improvement in economic efficiency, adverse trends in some basic macroeconomic aggregates have gained strength. What is especially disquieting are the low dynamics of exports to the European Union (UE) as well as the continued low level of exports to the Commonwealth of Independent States (CIS).

The favourable trends in 1Q00 include:
- double-digit (10.7%) industrial output growth,
- high growth of labour productivity in industry (18%) and lower unit labour costs,
- lower deficit in the general government budget and more restrictive budgetary policy compared to 1999.

Unfavourable trends include:
- further widening of the current account deficit (up to 9.5% of GDP),
- increase in the unemployment rate (13.9% at end-March, i.e. at a mid-1996 level),
- increase in inflation, as measured by the CPI, from 9.2% in 4Q99 to 10.3% in 1Q00,
- lower growth of real wages and social benefits,
- low general households' propensity to save,
- excessive inflow of portfolio capital,
- growth of nominal and real interest rates.

More restrictive macroeconomic policy

In accordance with earlier statements issued by the Ministry of Finance and the National Bank of Poland (NBP), the economic policy to be pursued in 2000 is more restrictive than that of the previous year. Fiscal tightening in the budget for 2000 is seen in a substantial reduction of the deficit with the Ministry of Finance planning to reduce the general government budget by 1.4 percentage point compared to 1999.

Moreover, the NBP, consistently aiming at an inflation target of 5.4% – 6.8% in December 2000, has again tightened its monetary policy which was reflected in another hike in interest rates in February 2000.

Return to the path of fast economic growth

Despite a tight macroeconomic policy, the Polish economy continues to exhibit a high growth rate. According to our estimates, GDP increased 6.0% in 1Q00 that is slightly less than in 4Q99 (6.2%). The high growth rate is, on the one hand, a result of a low base effect (1.6% GDP growth in 1Q99), but, on the other, influenced primarily by domestic demand, including the build-up of stockbuilding and improved performance of investment outlays.

Double-digit growth of industrial production

Like in 4Q99, industrial production in 1Q00 continued to increase at double-digit rates (10.7%). Growth in manufacturing was even higher, amounting to 11%. These results were achieved in a situation when employment in industry as well as unit labour costs fell and prices increased. What this all means is that firms' financial standing has improved, which may help to finance a significant increase in investment, in particular expected in the second-half of 2000.

Some basic indices of production in the construction sector have also improved. Although its growth rate was lower than that in 4Q99 (production increased 4.3% yoy), growth in labour productivity was higher and that of unit labour costs lower.

Unemployment

Last year's downward trend in labour demand in the industry sector has continued. According to the Central Statistical Office (CSO), employment in enterprises fell 3.6%, including a 6.5% decline in the industrial sector. The increase in employment in the sector of market and non-market services was not sufficiently high to ensure stabilisation in the labour market. As a result, registered unemployment rose to 13.9% by end-March 2000 – up from 13% at end-1999. By way of comparison, last year's unemployment rate was as low as 12.1%.

Growth in inflation

In March 2000, CPI rose 10.2% yoy. This means that price increases have slowed since they increased 10.4% in February. However, over 1Q00 the inflation rate was 10.3%, that is more than 1 percentage point higher than in 4Q99. The higher CPI was caused by higher-than-expected increase in food prices due to lower crops and state price intervention in the agricultural market, a rise in fuel prices, as well as the continued high growth of PPI.

What should be noted, however, is that in March 2000, PPI fell to 7.4% from 8.1% in February 2000 yoy. This significant decrease resulted primarily from changes in the time-table of introducing regulated price increases – particularly those in electricity and gas. Over the whole quarter, PPI increased 7.9% whereas in the previous quarter it increased 7.5%. As we already mentioned in the previous issue of PEO, growth of PPI under the given conditions of 1Q00 is quite favourable for businesses, but it may, however, make it more difficult to decrease the growth rate in the price of consumer manufactured products.

Low growth in household real incomes

The growth in unemployment made it possible to maintain a low increase in nominal wages. In enterprises, wages increased 15.4%, that is 4.6% in real terms. What should be emphasised is that in the first two months of 1999 the increase in average nominal pay was exceptionally low which led to a correspondingly higher growth in nominal pay in January and February 2000. This fact may be accounted for by the problems involved in the implementation of the reform of social benefits which have been gradually introduced since the beginning of 1999. Nevertheless, as early as March 2000 the wages increased 13.7% (3.2% in real terms). The lower increase in real wages is also due to higher inflation.

Lower labour demand, coupled with lower average real wages and low growth of nominal social benefits have all had the effect of considerably reducing the growth rate of real household income. The only component of household income to have led to a higher growth rate was the income from business activity. According to our estimates, real incomes in 1Q00 declined about 0.6%.

The continued lower households' propensity to save as compared with 1998 and 1999 became slightly higher than that in the previous two quarters. Together with the low rise in real incomes this helped to reduce the growth of private consumption.

Weaker domestic demand

The lower growth of consumption demand has led to weaker growth of domestic demand. The only components in aggregated demand to have increased are stockbuilding and investment. We estimate that the build-up in stockbuilding was responsible for 1% of GDP growth.

The increase in savings by enterprises as well as a significant inflow of foreign capital have made it possible to accelerate growth of investment outlays. According to our estimates, the volume of investment has increased about 12%.

Budget deficit

The 1Q00 turned out to be favourable for the budget, especially for the government budget. Faster economic growth and higher-than-expected inflation have enabled tax revenues to be increased. In addition, the financial standing of the Social Insurance Company (ZUS) improved since higher revenues were received due to a better collection of contributions and a higher economic growth in the situation when the low nominal rise in social benefits helped to limit higher spending.

Deterioration in the current account deficit

The 1Q00 yielded exceptionally poor export results. We estimate that since December 1999 the dynamics of Polish exports have been on the decline despite an economic recovery in the EU. According to NBP estimates, in 1Q00 the revenues from exports (in terms of US dollars) have decreased almost 10% yoy. In addition, the unclassified current account deficit (an approximation of cross-border trade balance) has deteriorated by about US$70 million yoy. It is mostly the significant weakening of the euro (its exchange rate against the dollar fell from 1.12 to 1.04 and 0.99 in 1Q99, 4Q99 and 1Q00, respectively) that was responsible for lower revenues from exports.

Imports registered a reverse trend as they increased 3.5% in 1Q00. As a result, the deficit in merchandise trade in 1Q00 was about US$3.8 billion, that is US$1 billion higher than that in the previous year.

The current account deficit of US$3.4 billion was more than US$1.2 billion higher yoy. What is most disquieting is that the deterioration in the deficit became more severe than that in 4Q99 when the deficit worsened US$0.7 billion yoy. At the same time we estimate that the share of the deficit in the current account has reached 9.5% of GDP.

In 1Q00 the balance of payments improved slightly. Despite a considerable current account deficit, high revenues from foreign direct and portfolio investment have made it possible to stabilise the official foreign currency reserves which have increased from US$25.5 billion at end-1999 to US$25.6 billion at end-March 2000.

Strengthening of the zloty

Relative stabilisation of the balance of payments in 4Q99 was not reflected in the exchange market. The following two elements affected the stronger position of the zloty since the beginning of 2000: high disparity in interest rates, increased following their respective rise in February, and information on the expected privatisation proceeds.

The rate of growth in money supply has decreased significantly from 19% annually by end-December to almost 14% by end-March. The rise in money supply rose partialy due to the Y2K problem in end-1999, whereas in 1Q00 it returned to the normal levels together with lower zloty-denominated deposits made by enterprises.

In 1Q00 household credits registered a slower increase. By end-December 1999 they were 53% higher (in nominal terms) yoy, whereas by end-March 2000 they increased more than 51%. At the same time, the growth rate of credits provided to enterprises slowed considerably. In 4Q99 these credits increased almost 22%, while in 1Q00 only 18%.

Summing up, in 1Q00 negative trends prevailed. Inflation was on the rise, unemployment and the current-account deficit also rose. In our opinion, the deterioration in the current account deficit is due to the monetary policy pursued by the NBP and accelerated privatisation. Paradoxically, the growth in basic interest rates together with the policy of the quasi floating of the zloty aimed at reducing both the internal demand and implementation of an inflation target, have led to a significant deterioration in the current account balance.

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Determinants of Poland's economic development

We have slightly changed the assumptions regarding the external environment compared to the previous issue of Polish Economic Outlook (1/2000). A bigger boost to the EU and continued high growth in the US are assumed. At the same time, we uphold our view on tighter budgetary and monetary policies in Poland. As in the previous issue, the forecast horizon extends up to the year 2001.

Trends in the world economy, 2000–2001[1)]

- **The US economy still booming**
- **The Euro–zone getting a firmer footing**
- **A broader based recovery in Asia and Latin America**
- **Further interest rates in the pipeline**
- **A continued slide of the euro**

Economic growth

The world economy is still improving and economic recovery reveals a broader based pattern. According to the general consensus, global growth should further accelerate until mid–year and then ease a little in the course of 2001. The IMF, in its latest World Economic Outlook, raised the world growth projection for 2000 up to 4.25% and pointed that risks are mainly on the upside. Growth in the US will be rather strong in 2000, though not as high as last year. Non–US growth is expected to accelerate further this year. The situation in the EU and Japan is believed to improve considerably though these economies will still lag behind the US – at least in 2000. The expected fall in oil prices and higher labour productivity should alleviate inflationary pressures, especially via producer prices. But faster growth and rising wages pose a potential threat of strengthening inflationary pressures. Therefore, a further tightening of monetary policy is in the pipeline this year. Along with more balanced economic growth in the US and the EU, the euro should strengthen in end-2000. However, the recent poor performance of the euro versus the dollar and the yen dashes hopes for a strong rebound. We do not see any serious threats to global economic development, besides the one mentioned in the previous issue of Polish Economic Outlook concerning a potential severe equity correction in the American markets.

USA

The US economy is still booming and there is scant evidence of its cooling down. GDP growth in 4Q99 was subsequently revised upward from 6.9% to 7.3% yoy. The 1Q preliminary figure points to 5.4% growth driven by consumer spending (8% growth). Surging domestic demand is a cause of growing imbalances in the economy, which are

1) Economic forecasts presented in this chapter constitute a consensus of leading forecasting centres (IMF, OECD, DIW, commercial investment banks, etc.).

mirrored among other things in a record high trade deficit (US$29.2 billion in February). Such strong demand is partly attributable to a wealth effect stemming from rocketing stock markets. Labour markets remain tight, although the unemployment rate rose to 4.1% in February and levelled off in March.

In order to secure a proper cooling of the economy, extremely careful macro-policy management is necessary as there are no signs of a self-induced slowing down of the economy and a reversing of severe imbalances. It is widely believed that only a significant slowdown in consumer spending can alleviate the problems. We believe that the Fed's tightening will finally put a lid on growth that should slow down in the second-half of the year.

The private sector balance sheet remains fairly robust, despite the fact that private savings have been on the decline and investment on the rise. This was possible due to a high valuation of assets. It makes many borrowers vulnerable to any corrections in asset prices and in particular those of stock markets such as the recent correction in the US equity markets of 14 April. It spread to other markets all over the world, which followed suit and saw declines. Technology shares were hit hardest. Although the initial losses were substantial by historical standards, indices rebounded quickly. However, this correction can undermine consumer confidence and limit the buying spree.

European Union

The economic slowdown of 1998–1999 seems to be over. Growth rates reach levels of those observed during peaks of previous cycles. Prospects are more favourable than they have been for a long time. Continued rising employment coupled with expected cuts in taxes in several countries will definitely bring about higher disposable income and boost consumer confidence. The ensuing higher consumer demand in turn will induce greater investment. Exports remain the driving force of growth as world GDP accelerates and the euro remains weak. The bullish US economy benefits European exporters by boosting external demand and keeping the euro low. This mechanism will lose momentum towards year-end. However, given the record of past growth rates and some structural rigidities in the EU, the growth rate could be expected to level off (see Table 1).

The outlook for Germany is very optimistic as favourable trends are strengthening. CPI, after a recent rise, is expected to decline from 1.9% yoy in March to something of 1% at the beginning of 2001 due to falling oil prices and moderate wage increases. The low budget deficit of 1.9% of GDP last year makes room for tax cuts. Moreover, unemployment is on the decline, however in March there was unexpected reversal (the first time in six months). It is believed to be a one-off rise. High readings for industrial output (3.4% mom sa in March) and manu-

Table 1. GDP in selected countries, 1996–2001 (% change yoy)

	1996	1997	1998	1999e	*2000f*	*2001f*
Global	4.3	4.2	2.5	2.7	*3.9*	*3.6*
OECD	2.9	2.8	2.0	2.7	*3.6*	*3.2*
USA	2.4	3.8	3.9	4.1	*4.5*	*3.0*
Canada	1.5	3.8	3.1	4.2	*4.3*	*2.9*
Japan	3.5	0.8	-2.9	0.3	*1.6*	*2.7*
European Union	1.7	2.6	2.7	2.2	*3.4*	*3.3*
Germany	1.4	2.3	2.0	1.4	*3.0*	*3.2*
France	1.5	2.3	3.2	2.7	*3.6*	*3.5*
Italy	0.7	1.5	1.3	1.4	*3.5*	*3.3*
United Kingdom	2.3	3.1	2.1	2.1	*3.4*	*3.0*
Russia	-5.0	0.9	-4.9	3.2	*4.0*	*4.5*
China	9.6	8.8	7.8	7.1	*7.0*	*6.5*

Source: IMF and forecasts derived from the McFair model devised at Yale University.
Notes: e – estimates; f – forecasts.

facturing orders point to an upward trend continuing in the course of 2000.

Italian economic growth in 4Q99 (2.1% yoy) was the highest since mid-1998, but still below expectations. Investment and exports were on an upward trend recording 6.6% yoy and 6.2% yoy increases. On the other hand, consumption remained sluggish (1% yoy). Both business and consumer confidence is improving giving hopes for a firmer rebound this year. Additionally, the outlook for inflation, which reached recently a three-year high, is positive. The latter should boost consumption that in turn would contribute to higher growth.

The UK economy experiences robust, though unbalanced, growth. The services sector is powering ahead and grows at a highest rate for three years. Whereas, manufacturing lags behind. Its output dropped for the third month in a row in February. This is partially attributable to the strong pound and thus weak exports. The latter coupled with surging domestic demand and robust imports led to the deterioration in the trade deficit. Generous public spending planned in the budget for this year may be a drag on growth of other GDP components. Tight labour market (the unemployment rate lowered to 4% in February – a 20-year low) and rising asset prices have contributed to buoyant private consumption.

CIS

The Russian economic recovery is on track. GDP expanded 3.2% in 1999 and a positive GDP figure is forecasted for this year. Still booming industrial production is a promising sign – 13% yoy during the January-February period. However, it must be borne in mind that up to April a low base effect is at work. High world oil prices and a weak ruble resulted in the record high trade and the current account surplus, US$35 billion and US$25 billion, respectively. Nonetheless, foreign reserves increased only a little in 1999 due to debt repayments, scarce foreign direct investment and outflows of portfolio capital. The situation improved in 1Q00, when gold and currency reserves rose from US$12.5 billion at the start of the year to US$15.5 billion as of 1 April.

The sustainability of growth depends on a pick-up in domestic demand. Although the economy grew by up to 8% (according to the preliminary estimates) in the year to the first quarter, it is hard to tell whether the rebound is self-sustained and whether it has any foundation other than high oil prices and devaluation. Economic prospects are still contingent on the successful implementation of structural reforms on public finances, banking and real sectors. These are essential to strengthen underpinnings of a market economy, and to provide a reliable legal framework. Provided these conditions Russia can regain foreign investor confidence and attract badly needed investment. Debt repayment will continue to be a drag on growth. In addition, the forecast of lower oil prices will put Russian in a less favourable situation than in the last year. Given these problems the outlook remains very unclear.

CEFTA

Prospects for the Czech economy are improving. The recent growth projections have been upgraded on the back of higher domestic demand and rising exports. The latter will probably contribute to an upturn in industrial production. Strengthening household consumption may widen the trade deficit gap that, on the other hand, can be subdued by higher exports.

Hungary continues to expand robustly. Growth has been driven by domestic demand and exports. Despite the positive export prospects the trade deficit is expected to enlarge due to increased growth of imports. In addition, export boost can be dampened to some extent by the recent appreciation of the forint. The beginning of the year marked an upsurge in industrial production of 17.7% yoy in January 24.9% yoy in February. Private consumption remains strong. Healthy economic expansion should help to bring further down the budget deficit to 3.5% this year from 3.9% last year.

Asia

The rapid recovery of the Asian economies is getting a firmer footing and has more of a broad-based pattern. Fast growth rates will exert their pressure on inflation. The growth will slow a bit in the course of the year, as stimulus stemming from dissavings, stock rebuilding, fiscal aid packages, and loose monetary policy will lose momentum. Moreover, the low base effect will cease to function. The unquestioned leader is South Korea with a 10.7% growth rate in 1999. Also Singapore, Malaysia, and Taiwan experience a V-shape recovery. The outlook for these economies remains promising provided they maintain a fast pace of structural reforms in the financial and corporate sectors. On the other hand, Thailand, Hong Kong, and Indonesia have not coped well enough with structural economic and social problem and thus experience slower growth rates.

The outlook for Japan continues to be mixed. On the positive side, industrial output and exports are on the rise driven by external demand, particularly from Asian economies. In March the Tankan survey indicated improving business confidence at major manufacturing sectors for the fifth time in a row. The trade surplus rose in February for the first time in 11 months but imports remained strong. An estimate of output in 4Q99 showing a contraction of 1.4% indicates that the recovery is not self-sustained. But once again a massive budget has been passed to boost the ailing economy. Surging public debt poses the greatest risk and may dampen the growth rate in the long run. This could lead to a sizeable reversal of the capital inflows observed since the beginning of 1998.

Domestic demand in China slowly recovers leading to a surge in imports (54.1% yoy in February). As export dynamics were lower (34.5% yoy in February), the trade surplus has started to decline. On the positive side, economic data point to a demise of deflation – CPI rose 0.7% in February and a positive figure is forecasted in March. Despite this inflationary monetary policy is expected to continue. Investment seems to bottom out and should accelerate in 2000. In addition, some structural reforms are underway spurred by prospects of higher competition due to a prospective WTO membership. This year the government will purse tighter fiscal policy aiming at reducing the budget deficit. As a result the GDP growth figure can be lower.

Latin America

The recovery in the region continues to unfold and becomes broad based. Domestic demand is, in general, the driving force accompanied by a rebound in investment. Also exports recorded some improvement due to higher international activity. However, given the limited openness of Latin America economies, trade is not going to play a decisive role. Higher commodity prices are still fostering the recovery and the importance of this factor remains significant. Tighter fiscal stance pursued by most governments in the region underpins the positive outlook. This coupled with reforms of public finances and its governance should contribute to continued betterment in investor sentiment. Despite the more favourable global economic conditions, the expected hikes in interest rates in the US are believed to make the recovery more difficult for they will drain Latin America of foreign investment. The longer the buoyant expansion of the US economy continues, the more likely is that economic revival in Latin America will be self-sustaining making the region less vulnerable to external factors.

Commodity prices

In 1Q00 the price of crude oil was significantly on the increase, ranging from US$24 to US$32 per barrel. This was due to the fall in crude oil reserves in the US responsible for 20% of the world's demand, and to the absence of any intervention on the part of the US Department of Energy. The world's oil reserves have systematically been on the decrease, and the gap between supply and demand has also widened. The period of cool weather in the northern hemisphere has also contributed to the increased demand for oil.

We expect that with the forthcoming warm season in the northern hemisphere and the continued loose discipline of production, the gap between demand and supply will narrow. It looks that as a result of the agreement on production quotas concluded in Vienna in March 2000, oil prices sustained within the range of US$22–26 per barrel are likely to persist. OPEC countries (except Iran), together with other oil producers, have agreed to have oil prices controlled through a flexible mechanism consisting in reducing production when these prices fall below a fixed variation band and in increasing production when the prices exceed the upper permissible limit. At the same time, oil producers have announced that they would pay careful attention to the problem of adjusting supply to demand and would make prompt interventions to redress balance in the markets.

Inflation

The outlook for inflation is rather positive. The recent drop in world oil prices due to increased production by OPEC members and expectations of a further decline should ease inflationary pressures. Also high labour productivity growth, globalisation, and new technologies could prevent excessive unit labour cost increases. Moreover, the recent hikes in interest rates in developed countries are to take their lagged effect this year. However, some threats are looming.

In the euro area, prices climbed gradually from 1.9% in January to 2.1% in March 2000, thus breaching the ECB's

Table 2. GDP deflator in selected countries, 1996–2001 (% change yoy)

	1996	1997	1998	1999e	*2000f*	*2001f*
OECD	1.5	1.4	1.0	1.0	*1.4*	*1.7*
USA	2.2	2.0	1.0	1.4	*1.9*	*2.1*
Canada	1.3	0.5	-0.6	1.7	*3.0*	*3.0*
Japan	-0.1	0.5	0.4	-0.9	*-0.7*	*0.1*
European Union	2.4	1.6	1.5	1.3	*1.8*	*1.8*
Germany	1.0	0.6	1.0	0.9	*1.0*	*1.8*
France	1.6	1.0	0.9	0.3	*1.0*	*1.2*
Italy	4.4	2.6	2.8	1.5	*2.0*	*1.7*
United Kingdom	3.1	2.2	2.5	2.9	*2.4*	*2.2*

Source: IMF and forecasts derived from the McFair model devised at Yale University.
Notes: e – estimates; f – forecasts.

Table 3. CPI in selected countries, 1996–2001 (% change yoy)

	1996	1997	1998	1999e	*2000f*	*2001f*
OECD	2.0	2.0	1.1	1.4	*1.8*	*1.6*
USA	2.9	2.3	1.6	2.2	*2.7*	*2.3*
Canada	1.6	1.4	1.0	1.7	*2.5*	*2.3*
Japan	0.1	1.7	0.6	-0.3	*-0.2*	*0.1*
European Union	2.1	1.8	1.4	1.3	*1.6*	*1.5*
Germany	1.3	1.5	0.6	0.6	*1.5*	*1.3*
France	2.0	1.3	0.7	0.5	*1.2*	*1.1*
Italy	3.8	1.7	1.7	1.7	*2.0*	*1.8*
United Kingdom	2.4	2.8	2.7	2.2	*1.8*	*1.8*
Russia	47.7	14.8	27.7	85.8	*16.0*	*11.0*
China	8.3	2.8	-0.8	-1.3	*0.5*	*1.0*

Source: IMF and forecasts derived from the McFair model devised at Yale University.
Notes: e – estimates; f – forecasts.

Table 4. Long-term interest rates in selected countries, 1996–2001 (%)

	1996	1997	1998	1999	*2000f*	*2001f*
USA	6.4	6.3	5.3	5.7	*6.8*	*6.8*
Canada	7.2	6.1	5.3	5.5	*6.8*	*7.0*
Japan	3.0	2.3	1.5	1.8	*2.0*	*2.6*
Euro area	6.2	5.7	4.7	4.6	*5.5*	*5.7*
United Kingdom	7.8	7.0	5.5	5.0	*5.5*	*5.3*
LIBOR (US$/year)	5.6	5.9	4.8	5.4	*6.5*	*6.6*

Source: IMF and forecasts derived from the McFair model devised at Yale University.
Note: f – forecasts.

target of 2%. Mainly high oil prices coupled with the weak euro are blamed for recent CPI readings. As they are expected to go down inflation should abate, however the weak euro gives rise to concern. Wage agreements in Germany turned out to be moderate despite aggressive demands on the trade unions side. On the other hand, higher growth and narrowing output gap should put pressure on prices, but this should not pose serious threats to general price stability.

In the US, inflation has been in check – however CPI March readings (0.7%) came above expectations. This may be the beginning of a higher inflationary period. Oil prices are believed to play a less significant role this year. On the other hand, wage pressures gain in strength given the tight labour market and exuberant growth. The employment cost index, which measures wages and benefits edged up 1.4% in 1Q00 – the biggest quarterly increase for a decade.

Interest rates

The ECB raised its interest rate twice this year. The first increase (from 3.25 to 3.5%) was announced on March 16. It was believed to be a pre-emptive measure aimed at cooling inflation. The decision was justified given the fact that the M3 growth rate was well above the ECB reference rate of 4.5% both in 1999 and in 1Q00 leading to a monetary overhang. Besides inflation remained at the target level. The ECB announced that it would remain vigilant on inflation due to edging up growth and the weak euro indicating further hikes to come. Next tightening took place on 27 March – another 25 basis points. It was spurred by a drastic drop in the euro exchange rate and the inflation rate above the 2% target. A weak euro poses threats to price stability despite moderate wage contracts and the forecast of lower oil prices. As the oil prices go down and the euro rebounds in the course of 2000, inflation prospects should improve.

Also the Fed increased its interest rates two times this year. The last time was on 21 March when the main rates were raised to 6.0% by a quarter point and the bank's discount rate to 5.5%. Limited signs of reining economic growth in and the prevailing imbalances are the main factors behind the decision. Experts expect further rate hikes before mid-year in attempt to cool the economy. A market consensus points to 0.25% hike on May 16 which seems certain in light of recent pickup in inflation and the employment cost index.

After a rise in interest rates by 25 basis points in February, the MPC of the Bank of England decided to leave the repo rate on hold at 6% during its April meeting. This was pretty much in line with market expectations though

Table 5. The volume of imports in selected countries, 1996–2001 (% change yoy)

	1996	1997	1998	1999e	*2000f*	*2001f*
Global	6.0	10.5	3.9	4.5	*8.9*	*8.0*
OECD	6.2	7.8	7.5	6.0	*8.0*	*7.0*
USA	6.4	14.3	10.6	11.7	*11.5*	*8.0*
Canada	5.1	12.6	5.8	9.7	*11.0*	*8.0*
Japan	10.3	2.1	-7.5	5.1	*12.0*	*14.0*
European Union	2.6	6.0	7.8	4.3	*6.2*	*5.3*
Germany	2.8	6.1	7.5	6.9	*8.0*	*7.0*
France	2.2	6.2	9.3	3.3	*8.5*	*5.5*
Italy	-2.0	3.6	6.1	3.4	*7.0*	*5.5*
United Kingdom	7.8	8.3	8.4	7.6	*7.0*	*4.0*
Russia	10.0	11.0	-16.0	-20.0	*9.0*	*13.0*
China	14.0	12.0	-3.8	8.0	*14.0*	*11.0*

Source: IMF and forecasts derived from the McFair model devised at Yale University.
Notes: e – estimates; f – forecasts.

some experts believe it was a mistake. Given the higher growth, tight labour markets, fiscal easing, and rising house prices more tightening is to come. Only when the MPC sees domestic demand slowing will it put rates on hold for this cycle.

Exchange rates

The IMF, in its latest World Economic Outlook, pointed that the prevailing misalignment of currency can be a potential threat to healthy development of the world economy. Current values of main currencies, i.e. the US dollar, the euro and the yen, do not match their fundamentals-indicated values. Thus, some corrections should be expected with an effect for the real sectors.

The euro has continued to slide further against the dollar. Since the middle of January it rose only once above the parity. The euro average rate dropped to 0.96 per dollar and to 102.6 per yen in March. It was even weaker in April reaching a lifetime low below 0.91. Still most experts believe in the narrowing-gap story, i.e. as the growth in the US slows and the European economy accelerates the euro will gain in strength against the dollar. However, recent developments indicate that capital flows and mergers and acquisitions play an important role. Thus, in the case of further hikes in interest rates, no substantial corrections in equity markets in the US, and the continued direction of mergers and acquisitions, the strengthening of the euro can be moderated.

In the first half of 1Q00, the yen experienced a decline from a very high value at end-December. This was caused by the shift in investor sentiment. Investors had become sceptical of the recovery setting in. As some signs of improvement have appeared in March foreign capital inflows resumed and drove the yen up. This mechanism is expected to be at works this year.

Forecast assumptions – domestic determinants

In the present outlook, we have assumed that there would be no currency crisis in Poland until end-2001. Despite a significant deterioration in the current account balance, we are of the opinion that faster growth of the world economy, restrictive economic policy and the planned sterilisation of privatisation proceeds in a special account with the NBP will make it possible to gradually diminish the threat of a currency crisis. We also assume that improvement in economic efficiency, reflected mostly in a dramatic reduction in unit labour costs and adjustment of Polish enterprises to the structure of demand in EU countries, will in effect bring about greater demand for Polish-made products in the second-half of 2000. We expect the dynamics of Polish exports to Russia and Ukraine to increase by 5% and 10% in 2000 and 2001 yoy, respectively. Detailed assumptions are given below.

We expect that in 2000–2001 the volume of foreign capital inflows (mostly due to privatisation) will increase and considerably more portfolio investments will be forthcoming in 2000. In addition, high interest rates in Poland will lead to a greater demand on the side of Polish enterprises for foreign credits. In anticipation of a possible reduction in interest rates the portfolio capital inflows may be stopped by end-2000.

The assumptions of our outlook for the years 2000 and 2001 are now presented in detail:

1. We assume that the government's short-term economic policy will aim at reducing both the current account deficit and the general government budget deficit. Our forecast is based on the following three assumptions underlying Poland's economic policy:

Table 6. Dollar exchange rate vs. the euro and the yen, 1996–2001

	1996	1997	1998	1999	*2000f*	*2001f*
Euro			1.11	1.07	*0.96*	*1.06*
Yen	109	121	131	114	*104*	*96*

Source: IMF and forecasts derived from the McFair model devised at Yale University.
Notes: 1. f – forecasts.
2. Annual averages.

(i) the NBP will keep its restrictive policy until 3Q00; the reduction in the NBP base interest rates can only be implemented after 3Q00,
(ii) the budget policy will aim at limiting the general government budget deficit, especially that of the government and ZUS (State Insurance Company) budgets; moreover we assume that an attempt will be made to minimise the financing of the deficit within the domestic financial system,
(iii) even in a new situation of a floating exchange rate introduced in the early 2000 we do not assume full liberalisation of capital flows to happen (despite Poland's earlier obligations towards OECD).

2. The costs of compulsory debt servicing to the Paris Club and the London Club as well as indebtedness of the private sector will amount to US$1.7 billion in 2000 and US$2.2 billion in 2001.
3. Labour force will grow 0.4 and 0.5, respectively.
4. The number of old-age pensioners and those who receive disability benefits will increase by 1.5% and 1.4%, respectively.
5. Average customs duties in trade with EU countries will be gradually reduced to 0%, whereas those with other countries will be maintained at a 1997 level.
6. Transfers from the EU will grow from about US$0.3 in 1999 to US$0.6 and US$0.9 billion over the next two years.
7. Foreign direct investment in terms of the balance of payments will reach US$9.0 and US$8.0 billion, respectively.
8. We assume that privatisation will accelerate and will be completed by 2001, privatisation proceeds amounting to 21 and 14 billion zlotys in 2000 and 2001, respectively.
9. The indexation of basic social benefits will be maintained; nominal average social benefits will increase 6% in 2000, and 7.5% in 2001.
10. In 2000 the personal income tax (PIT) rates will be maintained at 1999 levels, whereas corporate income tax (CIT) rates will be reduced by 3 percentage points, excise tax and VAT rates will remain at the level proposed in the draft of the 2000 Budget Act; in 2001 CIT rates will be further reduced by 4 percentage points and the PIT rates will be lowered to 18% and 28% as proposed in the government tax reform; finally the VAT base will be extended (in accordance with the government plan the VAT will cover agricultural and municipal sectors).
11. Employment in the state sector will be stable; an increase in employment will vary in the 0% and 3% range; we assume a fall in employment in the education and health care sectors and an increase in the broad administrative sector.

Center for Social and Economic Research

Analysis of the economic situation and outlook for 2000-2001

Domestic demand

- **Restrictive economic policy will weaken domestic demand in 2000**
- **Lower growth rate of real household incomes**
- **Weaker consumption demand**
- **Forecast of improved investment climate in 2000–2001**

Since 2Q99, economic growth has been on the increase. In 1Q00, this trend was arrested, when, according to our estimates, GDP registered an increase of 6%.

As in 1999, it was mainly domestic demand that drove Polish economic growth. According to our estimates, since 3Q99 domestic demand growth stabilised at 5.6 – 5.9%. Detailed data on growth of the basic components of aggregated demand are given in Table 7.

Domestic demand has continued to rise faster than GDP, and it was only in 4Q99 that the relation between these two rates was reversed. What this means now is that the Polish foreign trade balance has further deteriorated.

In this report domestic demand will be referred to as the sum of consumption and accumulation. Consumption is defined as the sum of households' consumption (i.e. the sum of consumption of households and that of non-commercial institutions) and public consumption (i.e. consumption of central and local government institutions). Accumulation is, in turn, defined as the sum of investment (gross outlays in fixed assets, gains in livestock inventories and intangible assets) as well as stockbuilding.

The fact that domestic demand growth has been arrested is the result of a gradually more restrictive economic policy. Monetary policy was the first to be tightened. Between September 1999 and February 2000, the NBP raised the base interest rates by 450 base points. At the same time, a budget was passed, which included components of direct and indirect fiscal tightening. Among the former ones were the assumed lower general government budget, lower nominal growth of wages in the government sector and lower social benefits. On the other hand, indirect components included firstly the rate of semi-annual inflation of 5.7%, established at an unrealistically low level.

After three quarters of faster growth of consumption demand, driven mainly by the increase in consumption credits, 1Q00 saw a much lower private demand which, according to our estimates, increased only 4.5% yoy. Lower private demand growth is due to a lower increase in real incomes. On the other hand, households' propensity to save has continued to be lower than that in the previous year.

In 1Q00, in contrast to last year, growth of investment outlays increased. We estimate that the outlays rose by

11.7%. Again the growth in investment outlays in machinery, equipment and transport has been on the increase, whereas that on buildings and construction continued to remain low.

Faster investment growth was caused mostly by an increase in enterprises' savings and by a larger inflow of foreign direct investment. The increase in these savings is a consequence of higher economic efficiency and improved price relations. Another important factor was the relative strengthening of the zloty resulting in lower growth of import prices.

Public consumption dynamics have continued to be slow since consumption has been increasing at a pace significantly slower than that of the other components of domestic demand. Tight fiscal policy and the price increases on goods and services purchased by enterprises in the

Table 7. Components of aggregate demand, 1997–2001

		GDP	Domestic demand	Households' consumption	Public consumption	Investment in fixed assets	Exports	Imports
1997	1Q-4Q	6.9	9.3	6.9	3.4	21.7	12.2	21.4
1998	1Q-4Q	4.8	6.4	4.7	1.8	14.2	14.3	18.5
1999	1Q-4Q	4.1	4.9	5.0	1.4	6.9	-1.5	1.9
forecast								
2000	*1Q-4Q*	*5.4*	*5.2*	*3.9*	*1.7*	*10.9*	*5.4*	*4.8*
2001	*1Q-4Q*	*6.3*	*6.8*	*4.9*	*2.0*	*13.7*	*8.6*	*9.8*
1997	1Q	6.9	7.9	6.7	3.5	19.6	11.3	23.8
	2Q	7.5	9.1	7.1	3.7	21.0	13.7	22.9
	3Q	6.7	9.4	7.0	3.6	21.2	6.7	19.0
	4Q	6.4	10.5	6.6	2.6	23.2	17.3	20.3
1998	1Q	6.5	7.2	6.2	2.4	17.3	26.6	34.5
	2Q	5.3	5.7	3.9	1.7	14.6	18.1	23.4
	3Q	4.9	6.1	4.3	1.6	14.2	14.7	17.2
	4Q	2.9	6.6	4.5	1.3	12.9	0.2	3.3
1999e1	1Q	1.6	3.3	4.3	1.4	6.1	-8.9	-2.8
	2Q	3.0	4.6	4.9	1.3	6.8	-3.5	2.4
	3Q	5.0	5.6	5.3	1.5	7.0	3.1	5.4
	4Q	6.2	5.8	5.4	1.4	7.3	3.8	2.7
2000	1Qe2	6.0	6.6	4.8	2.0	11.7	4.9	6.7
forecast								
2000	*2Q*	*5.0*	*5.3*	*3.9*	*2.0*	*11.9*	*4.2*	*5.4*
	3Q	*4.9*	*4.3*	*3.5*	*1.3*	*10.8*	*6.1*	*3.9*
	4Q	*5.7*	*4.9*	*3.4*	*1.3*	*10.0*	*6.4*	*3.3*
2001	*1Q*	*5.9*	*5.9*	*4.8*	*2.0*	*13.5*	*9.8*	*9.0*
	2Q	*6.6*	*6.9*	*5.1*	*2.0*	*15.2*	*9.0*	*9.5*
	3Q	*6.1*	*6.8*	*5.0*	*2.0*	*13.2*	*8.0*	*10.0*
	4Q	*6.5*	*7.4*	*4.7*	*2.0*	*13.3*	*7.7*	*10.6*

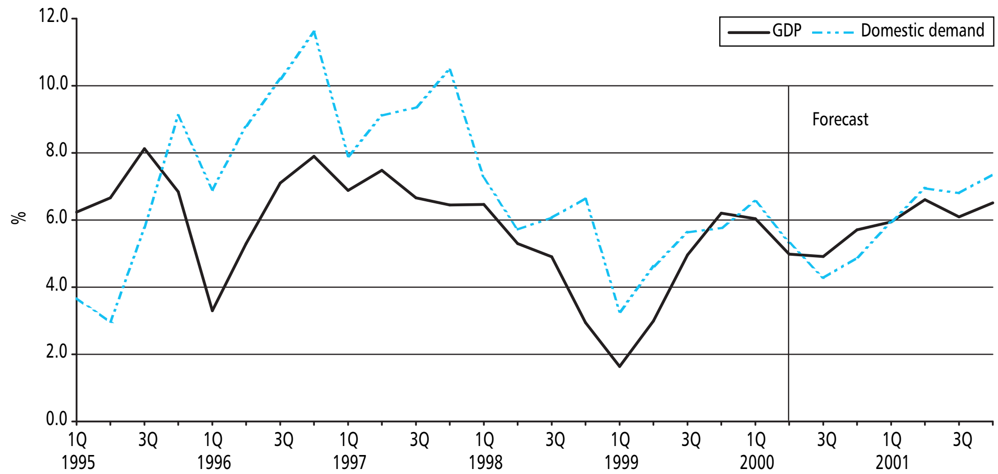
Source: Data and estimates (e1) – CSO; estimates (e2) and forecasts – CASE.
Notes: 1. Estimates in average prices of previous year.
2. Forecasts in 1998 average prices.
3. % change yoy.
4. Domestic demand is defined as the sum consumption of households, and non-commercial institutions, public consumption and investment. This table does not provide separate indicators for the consumption of non-commercial institutions.
5. Data are not seasonally adjusted.

government sector have additionally contributed to the slow rate of growth.

As in the previous issue of PEO, in this issue we expect GDP to amount to 5.4% in 2000, and to 6.3% in 2001. Our forecast is still more optimistic than the adopted 5.2% in the 2000 Budget Act, as well as the mean forecast for Poland published in Consensus Forecasting (5% and 5.2% for 2000 and 2001, respectively) in March.

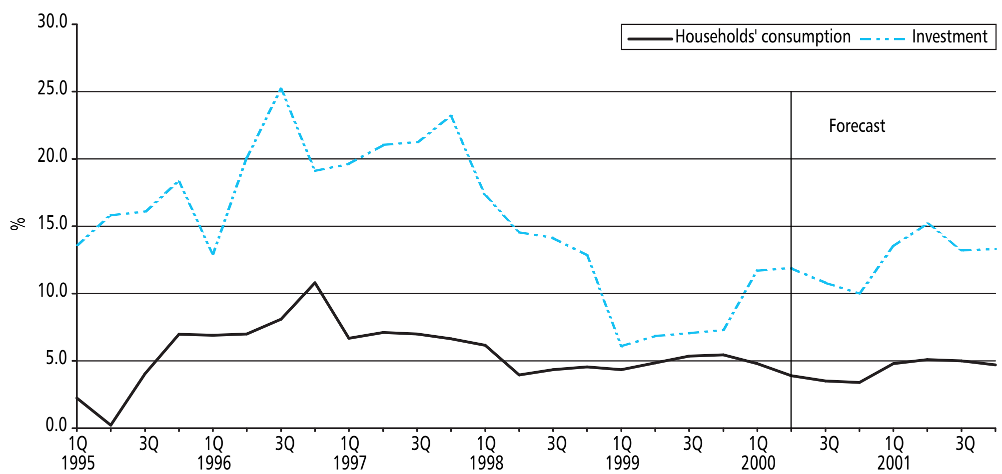
In our opinion, the upward trends and the structures of domestic demand registered so far cannot be maintained over a longer term in the future. They will be counterbalanced by the continued high level of nominal inter-

Figure 1. GDP and domestic demand, 1995–2001 (% change)



Source: CSO and CASE.
Note: CASE forecast starting from 2Q00.

Figure 2. Private consumption and investment, 1995–2001 (% change)



Source: CSO and CASE.
Note: CASE forecast starting from 2Q00.

est rates and the restricted fiscal policy. That is why we expect the structure of domestic demand to change. At the same time, we predict that domestic demand growth will increase from 4.9% in 1999 to 5.2% and 6.8% in 2000 and 2001 respectively.

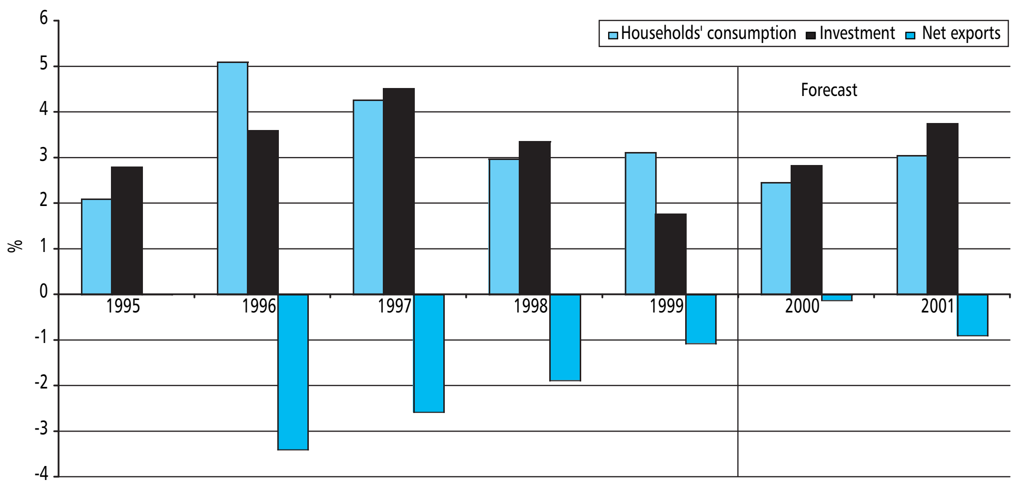
Unlike in the second-half of 1999, the first-half of 2000 will witness economic growth which will be affected by investment demand rather than by consumption demand. We also predict a slower growth of nominal household income due to slower increase in nominal wages in the government sector and in social benefits. The anticipated nominal pay increases and higher private-sector profits may turn out to be insufficient to compensate for the lower dynamics of budget transfers. In addition, high unemployment will have a dampening effect on excessively high pay rises. Combined with high inflation this will lead to a slower growth in real household incomes. It will only be in the second-half of 2000 that real incomes may see a higher growth rate as a result of

Table 8. Contributions to GDP growth, 1997–2001 (%)

	GDP	Households' consumption	Public consumption	Investment in fixed assets	Stock-building	Net exports	Exports	Imports
1997 1Q-4Q	6.9	4.3	0.6	4.5	0.1	-2.6	3.0	-5.6
1998 1Q-4Q	4.8	3.0	0.3	3.4	0.1	-1.9	3.7	-5.6
1999 1Q-4Q	4.1	3.1	0.2	1.8	0.0	-1.1	-0.4	-0.6
forecast								
2000 1Q-4Q	*5.4*	*2.5*	*0.3*	*2.8*	*0.0*	*-0.1*	*1.5*	*-1.6*
2001 1Q-4Q	*6.3*	*3.0*	*0.3*	*3.8*	*0.1*	*-0.9*	*2.3*	*-3.2*

Source: CSO (GDP) and CASE (other data).
Notes: 1. Contributions to GDP growth were calculated using the following formula:
*(annual increase of X / annual increase in GDP) * rate of growth of X.*
2. GDP growth and the sum of contributions to GDP may not add up due to approximations.

Figure 3. Contributions to GDP growth, 1995–2001 (%)



Source: CSO and CASE.
Note: CASE forecast starting from the year 2000.

the expected lower inflation. If, on top of that, the NBP succeeds in maintaining high interest rates an increase in the propensity to save may be envisaged. As a result, consumption demand over the whole year may rise 3.9% that is over 1 percentage point less than in 1999. In 2001, we may see a renewed reversal of this trend: the dynamics of real incomes may be higher, the propensity to save may also increase, whereas private consumption may be higher by 4.9%.

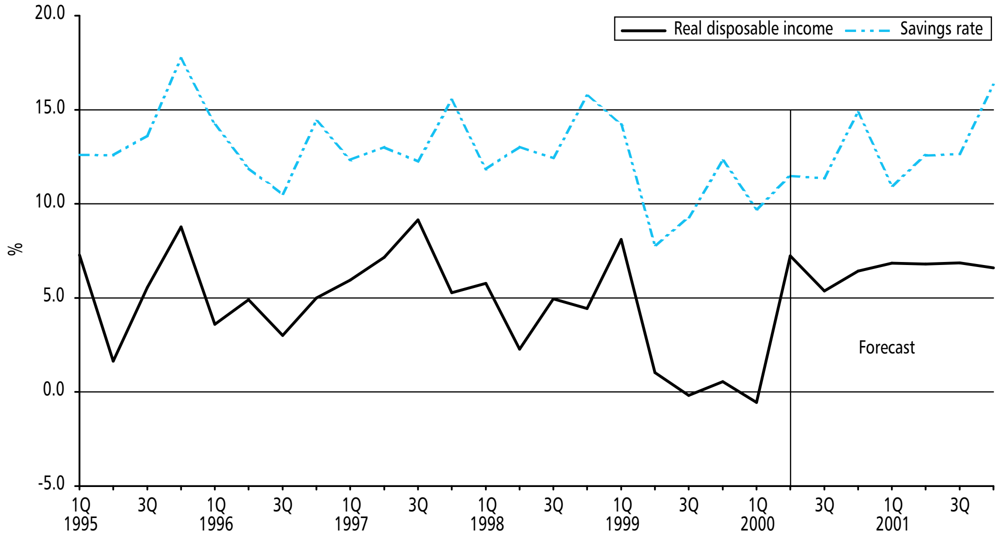
As much as consumption demand may prove to be weaker than in 1999, investment demand can be expected to increase significantly. The continued high volume of foreign investment, anticipated higher enterprises' savings together with lower prices of imported machinery and equipment will make it possible to accelerate the growth rate of outlays on fixed assets from more than 7% in 1999 to about 14% in 2001. Provided both the enterprises' economic efficiency and the investment efficiency

Table 9. Household disposable income, 1997–2001

		Disposable income	Wages and salaries	Social benefits	Savings rate	Real disposable income
		% change	% change	% change	%	% change
1997	1Q-4Q	23.0	23.8	19.7	13.2	7.1
1998	1Q-4Q	16.8	17.3	15.3	13.3	4.5
1999	1Q-4Q	9.7	10.7	9.1	11.0	2.3
forecast						
2000	*1Q-4Q*	*14.5*	*12.7*	*9.4*	*11.9*	*4.5*
2001	*1Q-4Q*	*13.3*	*13.0*	*9.0*	*13.2*	*6.0*
1997	1Q	24.2	23.0	19.0	12.3	6.0
	2Q	23.3	19.8	22.4	13.0	7.2
	3Q	24.8	25.5	22.3	12.3	9.2
	4Q	19.2	22.7	16.6	15.5	5.3
1998	1Q	20.5	20.9	17.0	11.8	5.8
	2Q	15.7	17.9	15.4	13.0	2.3
	3Q	16.7	15.5	14.1	12.4	5.0
	4Q	14.1	15.0	14.9	15.7	4.4
1999	1Q	14.8	9.1	10.9	14.3	8.1
	2Q	7.5	10.4	7.3	7.8	1.0
	3Q	7.0	11.4	9.5	9.3	-0.2
	4Q	9.8	11.8	8.7	12.3	0.6
2000	1Q	9.7	13.3	10.0	9.7	-0.6
forecast						
2000	*2Q*	*18.2*	*13.8*	*11.2*	*11.5*	*7.2*
	3Q	*15.6*	*11.8*	*8.0*	*11.4*	*5.3*
	4Q	*14.7*	*11.9*	*8.5*	*14.9*	*6.1*
2001	*1Q*	*13.9*	*11.3*	*9.0*	*10.9*	*6.1*
	2Q	*13.4*	*11.1*	*9.0*	*12.6*	*6.0*
	3Q	*13.3*	*11.1*	*9.0*	*12.7*	*6.1*
	4Q	*12.8*	*10.1*	*9.0*	*16.3*	*5.8*

Source: Annual data – CSO, quarterly data and forecasts – CASE.
Notes: 1. % change yoy.
2. The savings rate is shown as a percentage of nominal disposable income.

Figure 4. Change in household real disposable income and savings rate, 1995–2001 (%)



Source: CSO and CASE.
Note: CASE forecast starting from 2Q00.

improve, the ever growing share of investment in GDP may warrant a continued relatively high annual economic growth of 5–6%.

We expect the annual public consumption growth in 2000–2001 to stabilise at about 2%. Public consumption will thus constitute the component of domestic demand featuring the slowest rate of growth This will be due to the long-term policy of limiting the state's share in the creation and distribution of GDP.

A more restrictive economic policy, especially in 2000, than that pursued in 1999, may lead to a downturn in domestic demand in 2000–2001 below the GDP growth which, in turn, would enable macroeconomic stabilisation as well as balanced economic growth after 2001. The slower domestic demand growth will be offset by a faster growth of exports, which will make it possible to relatively improve the current account balance and stabilisation of the zloty exchange rate.

Beginning with the second-half of 2000 we also expect a stronger pro-export boost to appear for Polish-made goods in CIS countries – particularly in Russia and Ukraine.

Table 8 shows historical and forecast of contributions of the separate components of aggregated demand to GDP growth. The results of the decomposition of GDP growth should be interpreted in the following way: for example, in 1999 households' consumption would have led to a 3.2% increase in GDP, ceteris paribus. It should be borne in mind that the gain in a given aggregate should be related to the level of GDP in the previous year, and the sum total of growth rates of all the contributions (domestic demand, stockbuilding and foreign demand) should be equal to GDP growth.

In 2000, as a result of the anticipated weaker consumption demand we expect the private consumption contribution to GDP growth to temporarily diminish. It should be emphasised that in the years 1998–2001 the contribution of consumption in GDP growth will, on the average, be significantly lower than in the period of 1995–1997.

The predicted investment boom will make it possible again to increase the investment contribution to GDP growth in 2000–2001, which will be also greater than private contribution.

The upward trend in the foreign trade contribution, observed since 1997, is likely to be maintained till 2000. However, in the next year it is just as likely to decrease. We forecast that in 2000–2001 both the positive contribution of exports and the negative contribution of imports will be on the increase.

The slow upward trend in real household income has continued into 1Q00 (see Table 9). It resulted from the low dynamics of nominal and real wages, higher-than-expected inflation in the second-half of 1999 and the relatively small increase in real income due to business activity. The average pension has also decreased over the period of 12 months, although this decrease was only 0.1%.

We expect that beginning in 2Q00, the growth rate of real incomes will increase mainly due to the accelerated economic growth.

In 1Q00 net financial households' savings continued to be low. These savings were calculated in terms of the difference between the growth of the zloty and foreign currency deposits and cash in circulation and credit expansion).

In the period covered by our forecast we expect that households' propensity to save will continue if high interest rates are maintained. It is only in 2001 that the total households' savings rate (including such components as household investment or other forms of savings in addition to net financial savings) is expected to return to its 1997–1998 levels.

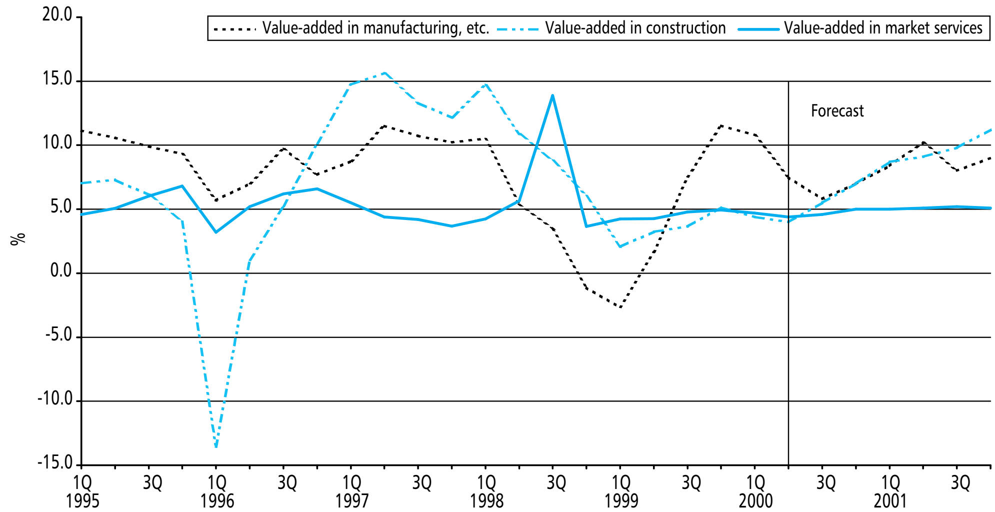
Value-added

- **Double-digit growth of industrial production**
- **Slower growth of construction output**
- **Market services as a stabilising factor of economic growth**
- **Faster growth of value-added in the years 2000–2001**

In 1Q00, growth of the value-added (according to our estimates at 5.7%) was lower than in 4Q99. We estimate that the value-added in non-agricultural sectors (i.e. excluding agriculture, forestry, hunting, off-shore and inland fishery) increased 5.9% yoy.

Growth of the value-added in industry, telecommunications and trade was higher than average. It grew slower than average in such sectors as construction and non-market services. The results of our estimates are shown in Table 10.

Figure 5. Value-added in major sectors of the economy, 1995–2001 (% change)



Source: CSO and CASE.
Note: CASE forecast starting from 2Q00.

The slower growth of exports in 1Q00 had an effect on the slower dynamics of industrial production compared with end-1999. Industrial output of enterprises employing more than 9 workers increased 10.7% yoy (see Table 11). At this point we would like to draw attention to the change in the statistics of the CSO. Until end-1999, short-term surveys included enterprises that employed more than 5 workers, whereas now only enterprises employing more than 9 workers. For the first time since 4Q97 mining output has increased (by 3.2%). At the same time, manufacturing output increased 11%, whereas that in the supplies in energy, gas and water rose by 12.2%. According to our estimates, the total value-added in industry was 10.8% higher yoy.

Table 10. GDP and value-added in major sectors of the economy, 1997–2001 (% change)

		GDP		Value-added				
				total	manufacturing, mining, water and gas supply	construction	market services	non-market services
		zloty billion	%	%	%	%	%	%
1997	1Q-4Q	469	6.9	6.5	10.3	13.6	4.4	3.0
1998	1Q-4Q	549	4.8	4.7	4.3	9.1	4.8	1.9
1999e1	1Q-4Q	612	4.1	3.8	4.7	3.8	4.6	1.3
forecast								
2000	*1Q-4Q*	*703*	*5.4*	*5.2*	*7.7*	*5.6*	*4.7*	*1.6*
2001	*1Q-4Q*	*797*	*6.3*	*6.1*	*8.9*	*10.0*	*5.1*	*2.0*
1997	1Q	103	6.9	6.4	8.7	14.7	5.5	4.7
	2Q	112	7.5	6.7	11.5	15.6	4.4	1.8
	3Q	118	6.7	6.4	10.7	13.3	4.2	0.7
	4Q	136	6.4	6.3	10.2	12.2	3.7	4.0
1998	1Q	123	6.5	6.4	10.5	14.7	4.2	3.4
	2Q	132	5.3	5.2	5.4	10.9	5.6	-0.2
	3Q	139	4.9	4.8	3.4	8.8	5.9	1.2
	4Q	155	2.9	2.8	-1.1	6.1	3.6	2.6
1999e1	1Q	134	1.6	1.4	-2.7	2.1	4.2	0.9
	2Q	146	3.0	2.8	1.6	3.2	4.3	1.0
	3Q	154	5.0	4.7	7.5	3.6	4.8	2.7
	4Q	178	6.2	5.9	11.5	5.1	4.9	0.9
2000	1Qe2	156	6.0	5.7	10.8	4.4	4.7	1.3
forecast								
2000	*2Q*	*168*	*5.0*	*4.7*	*7.5*	*4.0*	*4.4*	*1.5*
	3Q	*177*	*4.9*	*4.7*	*5.8*	*5.5*	*4.6*	*1.8*
	4Q	*202*	*5.7*	*5.5*	*7.0*	*7.0*	*5.0*	*1.8*
2001	*1Q*	*176*	*5.9*	*5.7*	*8.4*	*8.7*	*5.0*	*1.6*
	2Q	*191*	*6.6*	*6.4*	*10.2*	*9.1*	*5.1*	*2.0*
	3Q	*200*	*6.1*	*5.9*	*8.0*	*9.8*	*5.2*	*2.1*
	4Q	*229*	*6.5*	*6.3*	*9.0*	*11.2*	*5.1*	*2.2*

Source: Data and estimates (e1) – CSO; estimates (e2) and forecasts – CASE.
Notes: 1. Estimates in average prices of previous year.
2. Forecasts in 1998 average prices.
3. % change yoy.
4. Data are not seasonally adjusted.

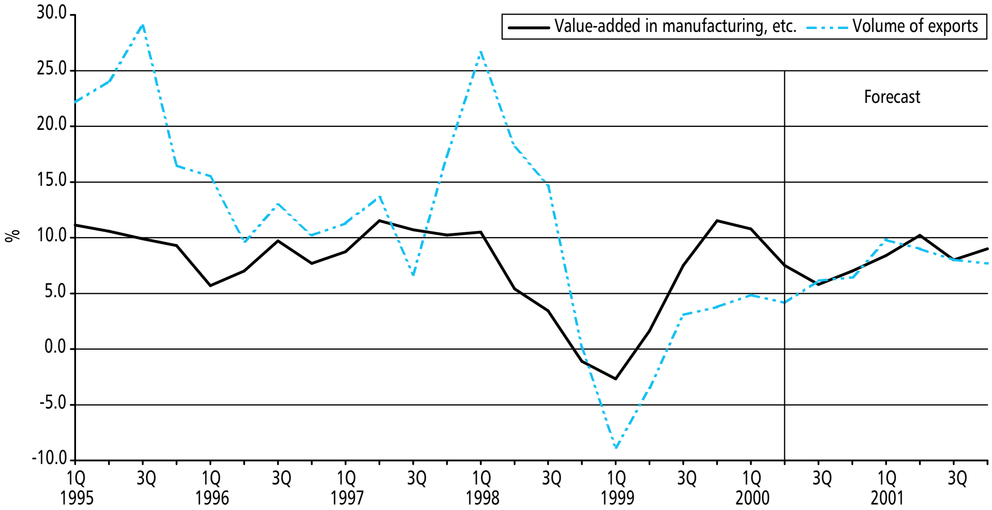
The growth rate in the construction sector declined considerably. In 4Q99 it was 6.2%, whereas in 1Q00 it fell to 4.3% despite generally favourable weather conditions. At the same time we estimate that the value-added in the construction sector increased 4.4% while that in the previous quarter increased by 5.1%.

Table 11. Selected short term indicators of the Polish economy, 1997–2001 (% change yoy)

		Output		Transport		Corporate sector	
		manufacturing, mining, water and gas supply	construction	freight	passengers	average employment	real gross wages
1997	1Q-4Q	11.5	16.5	1.5	-2.4	1.2	5.5
1998	1Q-4Q	4.6	11.4	-3.4	-2.9	1.5	3.7
1999e1	1Q-4Q	4.7	3.9	-4.0	-2.1	-1.2	3.0
forecast							
2000	*1Q-4Q*	*7.8*	*6.5*	*1.0*	*-1.2*	*0.3*	*3.5*
2001	*1Q-4Q*	*9.0*	*11.0*	*1.8*	*-0.2*	*0.0*	*4.5*
1997	1Q	7.9	19.6	3.6	-3.1	1.0	4.2
	2Q	13.9	24.9	2.8	-0.3	1.4	5.6
	3Q	11.8	13.3	-1.7	-5.2	1.7	6.7
	4Q	11.2	13.9	0.5	-2.3	0.6	5.3
1998	1Q	10.9	24.0	-5.6	-0.8	1.9	4.4
	2Q	6.0	10.2	-4.7	-3.4	1.7	3.3
	3Q	3.9	13.2	1.5	-2.6	1.0	3.6
	4Q	-0.8	4.5	-4.7	-4.4	1.6	3.7
1999	1Q	-3.1	0.6	-1.9	-2.6	-0.4	2.5
	2Q	1.2	4.0	-6.3	-2.5	-1.2	3.8
	3Q	7.5	3.2	-7.2	-1.6	-1.3	3.8
	4Q	11.7	6.2	-3.7	-0.3	-1.8	1.8
2000	1Qe2	10.7	4.3	-2.4	-0.1	-3.0	4.6
forecast							
2000	*2Q*	*7.5*	*5.1*	*-1.5*	*0.5*	*-2.5*	*2.7*
	3Q	*5.9*	*6.4*	*-0.7*	*1.0*	*-2.0*	*2.9*
	4Q	*7.1*	*7.5*	*-0.6*	*0.6*	*-1.5*	*4.2*
2001	*1Q*	*8.6*	*9.4*	*-1.0*	*0.4*	*-1.0*	*4.4*
	2Q	*10.3*	*10.1*	*-0.6*	*0.2*	*-0.1*	*4.4*
	3Q	*8.1*	*11.0*	*0.3*	*0.1*	*0.4*	*4.6*
	4Q	*9.1*	*12.5*	*0.8*	*0.1*	*0.6*	*4.7*

Source: Data and estimates (e1) – CSO; estimates (e2) with an exception of output and real gross wages, and forecasts – CASE.
Notes: 1. Data on construction and assembly and transportation calculated from the monthly data.
2. Changes calculated from data published in Statistical Bulletin (CSO).
3. Annual data on average employment relate only to enterprises classified as "large enterprises" (e.g. in industry – those with more than 5 employees until end-1999 and those with more than 9 employees since the beginning of 2000).

Figure 6. Value-added in manufacturing and volume of exports, 1995–2001 (% change)



Source: CSO and CASE.
Note: CASE forecast starting from 2Q00.

According to our estimates the value-added in services has registered a similar rise as that in the previous quarter. In market services it rose 4.7%, whereas in non-market services it increased 1.3%.

We expect that, as in the previous issues of PEO, the total value-added will increase 5.2% and 6.1% in 2000 and 2001, respectively. The growth rate of the value-added is likely to slow down until 3Q00, and then it will become faster. The expected acceleration in the growth may be caused by a faster rise in exports from the second-half of 2000 onwards.

The faster growth rate of the value-added in the nearest future will be made possible by the expected faster growth of the value-added in industry (7.7% and 8.9% in 2000 and 2001, respectively) and in the construction sector (5.6% and 10%, respectively).

The growth rate in the value-added in market services is expected to reach average 1997–1999 levels and will be more stable than that in other sectors of the economy. At the same time, in contrast to the years 1998 and 1999, it will be slower than the total value-added. We anticipate that telecommunications, trade, hotels will continue to feature fast growth, whereas transport and the services covering real estate and business will feature a slower growth.

According to our forecast the growth rate of the value-added in non-market services will continue to be slow. It is only after 2001 that this rate is likely to be higher (more than 2%) than that achieved in 1998.

Labour market

- **Continued downward trend of employment in industry**
- **Increase in unemployment**
- **Predicted stabilisation in the labour market in 2001**

In 1Q00, in addition to a seasonal decline in labour demand, the downward trend in employment, mainly in industry, continued. Moreover, the labour demand in other sectors of Polish economy diminished significantly; compared with the previous year market services registered smaller growth, and employment fell in the construction industry, whereas it stabilised in non-market services. According to our estimates, the average number of employed fell by 1.5% yoy (see Table 12).

Unemployment

In March 2000, the number of unemployed was 2533.6 thousand, i.e. it was 183.8 thousand higher (7.3%) than that at end-1999. Compared with the previous year, the number of unemployed was down 363.2 thousand, i.e. 16.7%. The unemployment rate amounted to 13.9% in March.

The situation in the labour market has been improving. By way of comparison, in March 1999 the number of unemployed was 339 thousand, that is 18.5% higher than that in December 1998. This means that unemployment has been growing at a slower pace than at the beginning of last year. The seasonal spring decline in the number of unemployed may be expected to be sharper than it was in 1999.

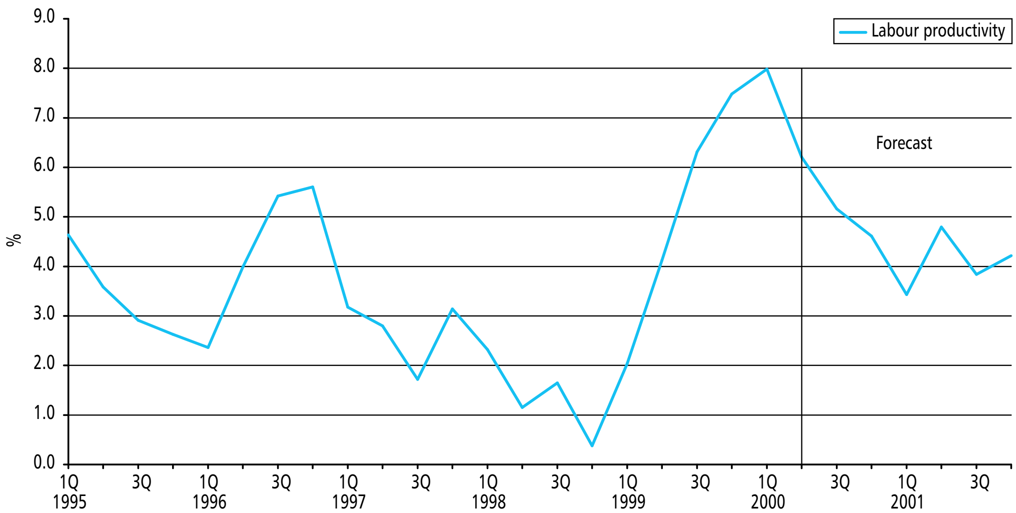
The previously noted downward trend in growth of the share of the unemployed that have not worked previously in the total number of unemployed has continued. In March this category of unemployed constituted 22.3% of all unemployed, that is 0.5% yoy. However, the share of graduates as a percentage of the total number of unemployed who have not worked previously has gone up from 27% to 24.9% yoy. This tendency follows the increased inflow of graduates into the labour market due to the population boom.

In March, the percentage of unemployed who were laid off due to reasons involving their place of work (the so-called "mass layoffs") was 7.5% compared with 6.5% in February 1999, which may be an indication of the accelerated processes of restructuring.

For the first time since June 1998, the consecutive months of 1Q00 saw a smaller number of registered new unemployed: the respective percentage figures were 77.0%, 80.3% and 90.2% yoy. It looks as if the previously noted upward trend in the number of people de-registering as unemployed has also continued throughout January, February and March, the respective percentage values being 109%, 101.6% and 99.5% yoy. We trust that the minimal decline in March was only an one-off effect. What seems to be a positive symptom in this situation is that the above tendencies have been associated with a growing number of people taking up jobs since the share of such people in the total number of de-registering unemployed has risen from 48.9% to 52.7%.

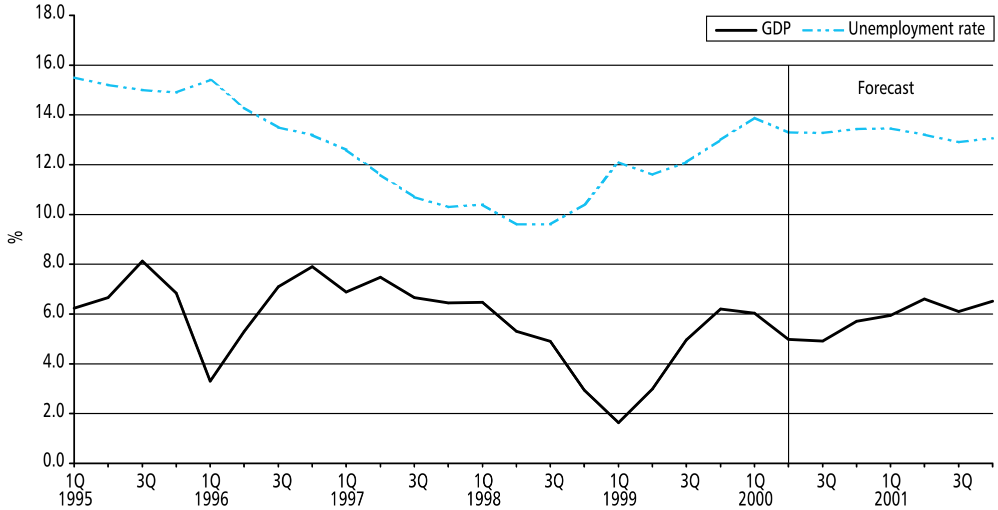
All the above facts seem to contradict the recent forecasts published by the Ministry of Labour that the unem-

Figure 7. Labour productivity in non-agricultural sectors of the economy, 1995–2001 (%)



Source: CSO and CASE.
Note: CASE forecast starting from 2Q00.

Figure 8. GDP and unemployment rate, 1995–2001 (%)



Source: CSO and CASE.
Note: CASE forecast starting from 2Q00.

ployment rate may be as high as 15% by end-2000. According to our predictions this rate will not be higher than 13.4%.

Some selected aspects of the projected reform in the labour market (short commentary)

At the turn of March and April 2000 negotiations were started on the government's programme to fight unemployment. The principal aim of this long-term project is to increase the activity from the present 58% to 62–64% in 2006. In addition to some measures that are meant to improve the quality of the labour force in Poland through the reform of the education system and to make the labour market more flexible through the reform of the Labour Code, as well as those aiming at lessening the tax burden on employers, especially small and medium-size businesses, the programme includes an differentiation in minimum wages depending on the age of the employee. This item is of special importance in view of the expected higher inflow of young people into the labour market in the next few years. At the present time, minimum wages in Poland, set by the Ministry of Labour quarterly, are paid to all full-time employees in the whole country. They currently amount to 700 zlotys, which is something of 36% of the average pay. If minimum wages are related to their median value, which seems to be a more reasonable approach in the case of an asymmetric distribution of wages, then we find that in 1997 (according to the OECD research) the minimum wages in Poland constituted 44.6% of the median wages and as much as 78.3% of the low wages median (low wages represent the bottom quintile of the distribution). By way of comparison, the above values were respectively 37.4% and 71.9% in Hungary, and 21.2% and 34.6% in the Czech Republic. It seems, therefore, that minimum wages in Poland are relatively high compared with other countries of the Central Europe. Poland, as well as the other countries mentioned above, does not make any distinction in wages depending on age or region. This form of differentiation is, however, employed in many OECD countries. Lower minimum wages are paid to young workers in Belgium, Luxembourg, the Netherlands, Portugal, Ireland, the United Kingdom, and New Zealand. Regional differentiation is also found in Canada, the USA and Japan. It seems that both these forms of differential have much to recommend them in Poland. This is because due to the aforementioned demographic processes and also due to a high regional differentiation in the labour market.

Is it technically feasible to implement the main aim of the reforms of increasing the activity rate from the present level of 58% to 62–64% in 2006? At the present moment Poland's situation in this respect looks much more favourable than that in Hungary where the above rate is 53%, but it is less favourable than that in the Czech Republic where the activity rate stands at 66%. The efforts at increasing the activity rate would mean that Poland wants to follow the example of such countries as the USA or Japan, which have succeeded in increasing this rate from about 70% to 75% in the last decade. On the other hand, the activity rates in EU countries have declined from 59–60% to 56–57% over the same period. This means that the present rate in Poland does not differ much from European standards, and therefore any effort to have it increased, beneficial as it may be, is likely to prove extremely difficult.

Table 12. Components of the labour market, 1997–2001

		Employment		Registered unemployment	Unemployment rate
		thousand	% change	thousand	%
1997	1Q-4Q	15439	2.8	1826	10.3
1998	1Q-4Q	15800	2.3	1831	10.4
1999	1Q-4Q	15658	-0.9	2350	13.0
forecast					
2000	*1Q-4Q*	*15556*	*-0.7*	*2447*	*13.4*
2001	*1Q-4Q*	*15756*	*1.3*	*2397*	*13.1*
1997	1Q	15048	2.5	2236	12.6
	2Q	15374	3.0	2040	11.6
	3Q	15594	3.4	1854	10.7
	4Q	15739	2.3	1826	10.3
1998	1Q	15506	3.0	1846	10.4
	2Q	15819	2.9	1688	9.6
	3Q	15921	2.1	1677	9.6
	4Q	15953	1.4	1831	10.4
1999	1Q	15423	-0.5	2170	12.1
	2Q	15680	-0.9	2074	11.6
	3Q	15748	-1.1	2178	12.1
	4Q	15782	-1.1	2350	13.0
2000	1Q	15185	-1.5	2509	13.9
forecast					
2000	*2Q*	*15518*	*-1.0*	*2397*	*13.3*
	3Q	*15678*	*-0.4*	*2408*	*13.3*
	4Q	*15845*	*0.4*	*2447*	*13.4*
2001	*1Q*	*15405*	*1.4*	*2449*	*13.5*
	2Q	*15678*	*1.0*	*2397*	*13.2*
	3Q	*15888*	*1.3*	*2358*	*12.9*
	4Q	*16055*	*1.3*	*2397*	*13.1*

Source: Annual and quarterly data with an exception of employment data – CSO; quarterly employment data and forecasts – CASE.

Employment in enterprises

As mentioned earlier, the CSO has changed its statistical base which served to calculate the number of people employed and those working. In the statistical analysis small enterprises that operate in the services sector have been excluded. The development of enterprises of this kind is not only fully consistent with the logic of economic processes, but it has also become a government priority in the last few years. It means that the GUS data will fail to include the enterprises that should have and are most likely to have the largest share in employment in the years to come.

In 1Q00, employment in enterprises (in comparable terms) was 74.5 thousand (1.3%) smaller than in December 1999. In other words, it fell 3.5% yoy in March, which is tantamount to the unexpected acceleration of decline in employment. Since July 1999 employment in the 12-month period has been found to fall by not more than 2%.

The above decline seems to be due to two types of trends that were noted at the beginning of 2000. First of all, a marked acceleration has appeared in the process of reducing employment in the sectors that had been undergoing restructuring. For example, in March 2000 employment in the metallurgical industry was 19.3% lower yoy. Last year a similar index had the average value of 10.1%. At the same time, employment in services has been growing at a much slower pace than in previous years. For example, since beginning-1996 employment in trade and repairs has seen the slowest increase of only 0.2% over the whole year as compared with the average value of 7.3% of the last year. These results may be a consequence of the new regulations on paying social benefit contributions by full-time employees. It may be that some employees who have been employed under these conditions have had to hide in the grey sphere, which may apply mostly to those employed in the services dealing with real estate and business where various contracts on mandate used to be especially popular.

Wages

The problem of a narrower statistical base used by the CSO also applies to wages. Therefore, the absolute figures published in 2000 cannot be used for comparison with those in the previous year. If, on top of that, we realise that the 1999 data cannot be compared with the 1998 data due to the fact that, as a result of the pension reform, wages became presented in their gross values, we can easily image the range of difficulties that are encountered if we want to make an analysis of the problem of wages in Poland over a longer term with the use of the CSO data.

With all these changes taken into account, nominal wages have been found to increase 13.7% yoy in March. This yields a real rise in wages of about 3.4%, which means that the negative scenario presented in the previous issue of PEO has come true. The arrested growth of real wages at end-1999 did not result, unfortunately, from the deterioration in the labour market, rather it was due to a higher-than-expected inflation. We expect that real wages will be growing faster before year-end. This will be mostly an effect of the improvement in economic performance and the continued fast increase in labour productivity.

Unemployment benefits

The upward trend, observed since the second-half of 1999, in expenditures on unemployment benefits has continued. In March 2000 they were 25.5% yoy higher (in real terms), which is obviously involved with the much higher growth of the number of unemployed. What should, however, be emphasised here is that the amount of the basic benefit has decreased 3% (in real terms), which seems to be quite a positive outcome. High unemployment benefits are the main cause of low activity of unemployed in job-seeking. In Poland, the opinion is still popular that the very fact that a person registers at the employment office is equivalent to his or her undertaking job-seeking. Nothing could more false. An average unemployed American devotes about 40 hours weekly to job-seeking, whereas an average Pole spends only 4 hours on the activity of this kind.

Prices

- **Further growth of inflation**
- **Increase in core inflation**
- **Forecast of a beginning of decline in inflation by August-2000**

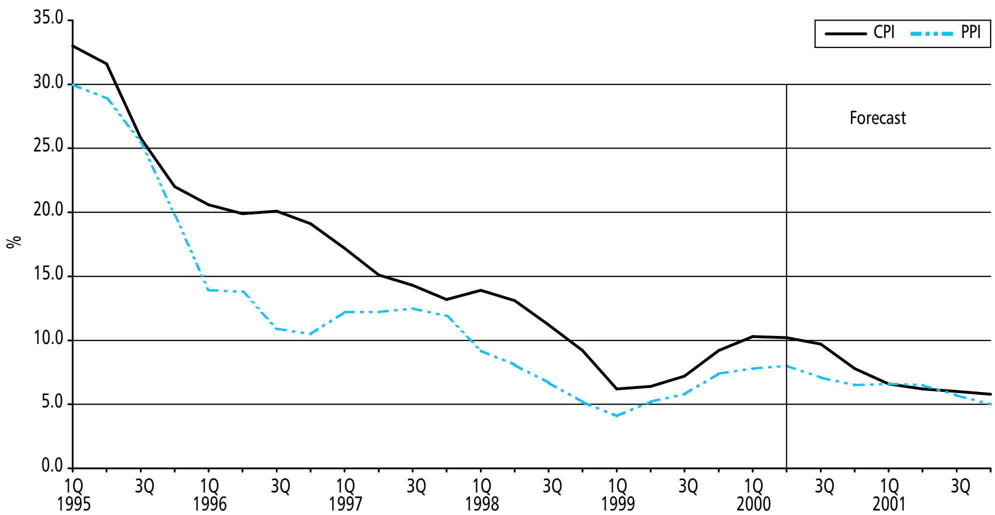
In 1Q00, the inflation rate was again on the increase. The Consumer Price Index (CPI) increased 10.3% yoy, whereas in 4Q99 it rose 9.2%. The Producer Price Index (PPI) increased 7.8%, whereas in 4Q99 it rose 7.4% (see also Table 13).

In 1Q00, food prices grew by 7.7% January-on January, 8.9% by February-on-February and 9.2% March-on March. It is clear, therefore, that the upward trend of the second-half 1999 continued. What should be noted, however, is the gradual decline in monthly increases, which were 1.4%, 1.1% and 0.9% yoy in January, February and March, respectively. A slower upward trend in the growth of food prices has been observed. This was caused by gradually lower increases in fruit and vegetable prices and poor crops in 1999, as well as by stable meat prices due to an oversupply. Similar price trend as in prices of fruits and vegetables was observed for other foodstuffs. Faster rises in the prices of bread and cereal products, due to the continued growth of corn prices resulting from a lower supply, has also been notched up. In this situation, the Agency of the Agricultural Market (ARR) made a decision to sell corps in the market in March 2000. As a result, corn prices both in agricultural stock-markets and other marketplaces stabilised, and later began to fall slightly.

The prices of non-food products increased by 10.9%, 10.7% and 11% yoy in January, February and March, respectively. These increases were higher than those in 4Q99 and were due mostly to higher crude oil prices in world markets and to higher excise tax on fuels in Poland. As a result, average fuel prices have risen by 7% since December 1999. In addition, a considerable rise in prices of medicines has also been registered. The strong zloty through import prices and PPI, as well as the slower growth in money supply and stabilisation of the growth of consumption credits have all had a deflationary effect (see the paragraph on monetary policy).

The prices of services increased 11.9% January-on-January, by 11.8% February-on-February, and 10.7% March-on-March, whereas monthly increases were 3.0%, 0.9% and 1.0% in January, February and March, respectively. In the whole 1Q00, these prices rose by 5.0% compared with 6.4% yoy. The slower rate of growth in 2000 stemmed from a different time-table of government-controlled increases in energy prices. In 1Q00, lack of agreement between power stations and the Office of Energy Control (URE) made it impossible to introduce higher energy prices, and therefore this decision was postponed until 2Q00. Price increases in 1Q00 were partly generated by a considerable rise in transport services, which were 5.2%, 2.3% and 0.9% in January, February and March, respectively. These increases were caused by growing fuel prices. In addition, charges for renting flats,

Figure 9. CPI and PPI, 1995–2001 (% change yoy)



Source: CSO and CASE.
Note: CASE forecast starting from 2Q00.

as well as gas and cold and hot water charges also increased significantly.

In 1Q00, the PPI amounted to 8.1%, 8.2% and 7.4% in January, February and March, respectively. In the first two months of 2000, the PPI were mainly affected by the rising prices of raw materials and the weak zloty in 4Q99. However, the March data provided confirmation that despite a higher excise tax the downward trend in the PPI continued probably mostly due to a stronger domestic currency at end-1999 exerting a deflationary effect on the PPI by way of import prices. Another reason may lie in the decline in inflow of industrial orders, proved in the business survey. This is a result of some slowdown in domestic demand as expected by producers.

We expect the dynamics of monthly increases in food prices to slow down. However, these increases will contin-

Table 13. Basic price indicators, 1997–2001 (% change yoy)

		Price indices				Currency basket	GDP deflator
		CPI	PPI	exports	imports		
1997	1Q-4Q	14.9	12.2	12.9	13.6	16.0	14.0
1998	1Q-4Q	11.8	7.3	6.8	2.4	6.1	11.7
1999	1Q-4Q	7.3	5.6	7.9	7.0	10.3	7.0
forecast							
2000	*1Q-4Q*	*9.5*	*7.7*	*5.0*	*4.8*	*2.1*	*8.4*
2001	*1Q-4Q*	*6.2*	*6.0*	*6.4*	*6.2*	*5.9*	*5.8*
1997	1Q	17.2	12.2	11.7	13.0	13.6	13.8
	2Q	15.1	12.2	11.9	12.2	14.3	13.2
	3Q	14.3	12.5	13.6	15.0	18.1	13.4
	4Q	13.2	11.9	14.3	14.2	17.6	15.2
1998	1Q	13.9	9.2	10.4	9.9	13.1	11.8
	2Q	13.1	8.1	8.1	3.2	6.7	12.0
	3Q	11.2	6.7	6.0	-0.1	3.9	11.9
	4Q	9.2	5.2	3.9	-1.4	1.6	11.3
1999	1Q	6.2	4.1	8.0	2.7	9.0	7.1
	2Q	6.4	5.2	7.0	7.3	12.5	7.1
	3Q	7.2	5.8	4.7	6.6	7.7	5.8
	4Q	9.2	7.4	11.8	11.3	11.5	7.6
2000	1Qe	10.3	7.8	7.0	7.2	1.9	9.8
forecast							
2000	*2Q*	*10.2*	*7.8*	*4.0*	*4.8*	*1.8*	*9.4*
	3Q	*9.7*	*8.0*	*6.6*	*6.2*	*3.8*	*8.2*
	4Q	*7.8*	*7.0*	*2.5*	*1.2*	*0.8*	*6.8*
2001	*1Q*	*6.6*	*7.0*	*6.5*	*6.9*	*7.2*	*6.6*
	2Q	*6.2*	*6.4*	*6.9*	*6.8*	*6.7*	*6.0*
	3Q	*6.0*	*5.3*	*5.7*	*5.5*	*5.4*	*5.7*
	4Q	*5.8*	*5.2*	*6.5*	*5.5*	*4.5*	*5.2*

Source: Annual data – CSO; currency basket – NBP; GDP deflator, estimates (e) with an exception of CPI, PPI and the currency basket, and forecasts – CASE.

Note: Currency basket over 1996–1998 consists: 55% of US$ and 45% of DM, and from 1999: euro – 55% and US$ – 45%.

ue to be much higher than those in the previous year due to the further rise in fruit and vegetable prices and a slight acceleration in meat prices which has been found to be rising as a result of lower live-stocks of swine and cattle. Given higher demand from Poland's eastern neighbours food prices are likely to register faster growth. The prices of processed cereal products may also increase as a consequence of higher corn prices, although they seem to have lost their previous impetus and will end up at a stable level.

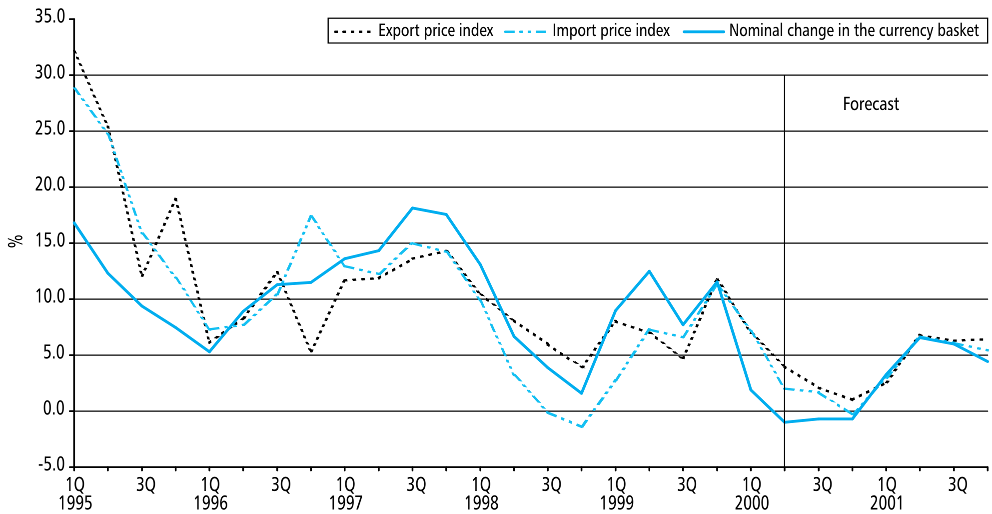
In the nearest future the prices of non-food products are likely to feature a downward trend as a result of the effects of the stronger zloty in 1Q00 and, consequently, lower PPI. In addition, the results of the policy of increasing the base interest rates by the Monetary Policy Council (MPC) will continue to be perceived in the form of a slowdown of M2 monetary aggregate and lower growth of consumption credits. Additional moderate rise in real wages is also likely to contribute to the fall in the prices of non-food products.

In our opinion, in 2Q00 the prices of services will be affected by energy prices to be raised in June 2000, whose share in the total CPI is now 3.4%. With the expected hike in these prices by 12% their additional contribution would amount to about 0.4%. On the other hand, the growth rate of fuel prices will be smaller, and as a consequence, the rise in transport services should be halted.

We expect the PPI to fall in April and May 2000 as a result of the effects of the stronger zloty at the beginning of 2000 and lower orders in industry stemming from the demand adjustment. One should, however, expect that at the turn of 2Q00 and 3Q00 the so-called base energy prices will be raised by some 12%. With their 10% contribution the increase in PPI will be more than 1%. Since energy prices are an important component in the enterprise's calculation of its costs a higher rise in PPI can be expected than what could come as a result of the share of energy prices in the price basket. The effects of the weaker zloty in April 2000, which should boost the PPI, should not be perceived until 4Q00 and 1Q01.

We forecast an increase in CPI to 7.3% in December 2000 taking into account the latest change in the price basket and the recalculated 1999 base of price rises. The annual average rise in 2000 may be as high as 9.5%, whereas that in 2001 may drop to 6.2%. A similar downward trend is expected for PPI to reach 7.7% and 6.0% for 2000 and 2001 respectively.

Figure 10. Export and import price indices and nominal change in the currency basket, 1995–2001 (% change)



Source: CSO and CASE.
Notes: 1. CASE forecast starting from 2Q00.
2. Currency basket over 1996–1998 consists: 55% of US$ and 45% of DM, and from 1999: euro – 55% and US$ – 45%.

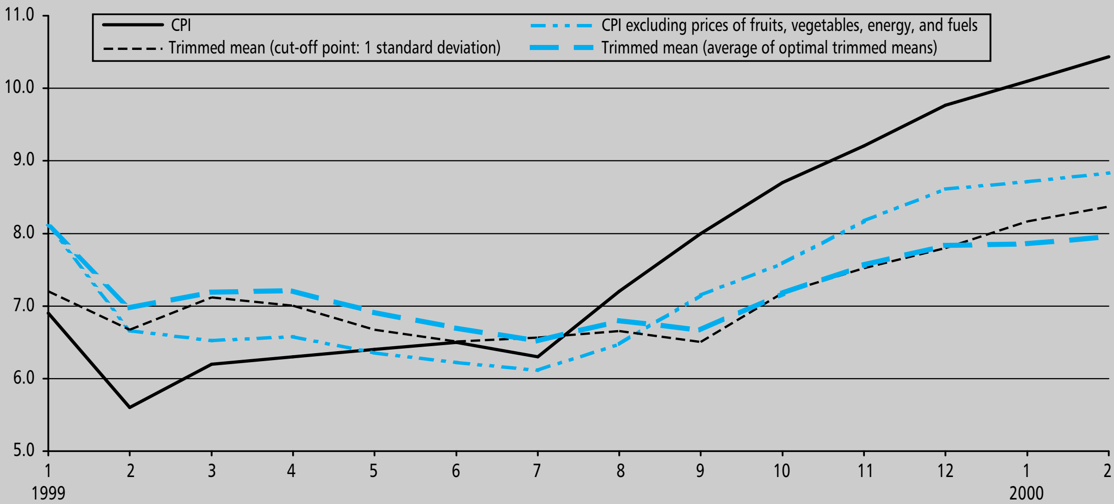
Core inflation

In 4Q99, core inflation stabilised at 8% over the 12-month period. The figure shows several alternative estimates of core inflation such as the trimmed mean (cut off point – 1 standard deviation) and arithmetical average of 5 trimmed means optimal for various time horizons. The indexes thus obtained reflect inflation pressures in the short and medium run. By way of comparison, two additional curves are also shown: the commonly used Consumer Price Index (CPI), and the index calculated with exclusion of prices of fruits, vegetables, energy and fuels. The latter has weaker theoretical foundations and does not meet all the necessary requirements of a core index, and therefore should be used only with caution in the diagnosis of demand pressures in economy.

All the indices have indicated that core prices are relatively stable. In the situation of continually rising CPI this means that the discrepancy between the conventional and core indices has widened. The difference provides information on the expected trends in the CPI: when the curve representing the CPI lies above the curves for core indices (the current situation) a downward trend in the Consumer Price index can be envisaged. These predictions are confirmed by the analysis of the disaggregated CPI values. What follows from this analysis is that the high growth of the 12-month CPI (by end-February 2000) mainly stems from higher prices of potatoes (increase by 90% yoy) and fruits (increase by 40% yoy) as a result of poorer crops, and of higher fuel prices (by 56%) following the rise in world's prices. An additional boost to price increases was given by a series of hikes in administrative and quasi-administrative price increases, e.g. radio and television fees (23%), liquid gas (48.5%), pluming services (28%), cold water (22%) and other types of services such as house rents. All these changes are the result of classical, mostly reversible, supply shocks of seasonal, administrative or fuel nature and provide very little information, in any, on changes in the state of demand pressures in economy (at least over a short period of time).

This very nature of the shocks that triggered the increases explains why the above mentioned increases that have been "pulling up" the CPI over the first few months of 2000 did not translate into core indices and, at the same time, they have led to gradual disappearance of the secondary effects of supply shocks that were responsible for their growth in 4Q99. Therefore, changes in core price indices and the analysis of individual changes in the components of the price basket allow to make cautious forecasts of gradual stabilisation, and, in the longer run, for decrease in the CPI dynamics.

Core inflation, 1999–2000



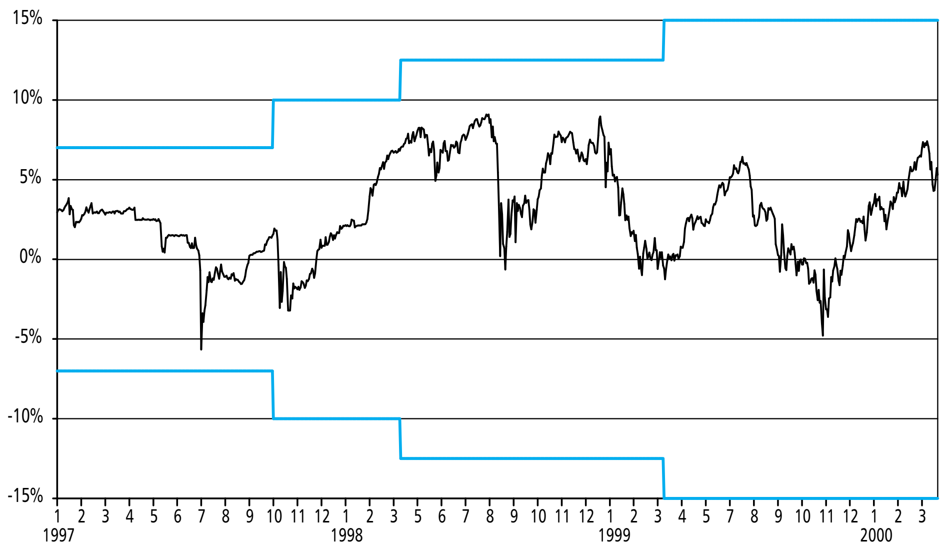
Source: Author's calculations.

Exchange rate

- Exchange rate movements
- Inflow of short-term capital and strong appreciation of the zloty
- Floating of the zloty in 2Q00

In 1Q00, the foreign exchange market was influenced by every possible domestic and foreign political and economic factor – both positive and negative. As a result, the zloty exchange rate against the dollar and the euro fluctuated sharply, with a general trend to strongly appreciate. These movements became more pronounced when the Council of Ministers and the MPC made a decision on April 11, 2000, to fully float the zloty. Interest rate disparity following the December rise in interest rates was a sufficient incentive for short-term capital inflows to appear, which strengthened the zloty at end-January when the deviation of the euro-dollar basket from the central parity surpassed 4%. Information on the poor results of Poland's foreign trade and inflation hovering around 10% provided a persistent stimulus strong enough to cause a temporary weakening of the zloty. By late January 2000, the currency market, by taking advantage of favourable production results in 4Q99 and the fact that Mr Wąsacz had retained his ministerial post, was able to strengthen the zloty again. However, after Warsaw power stations had been privatised without recourse to having foreign currencies exchanged in the interbank market, the process of appreciation of the zloty was halted. The announcement of a rise in interest rates has alternately weakened and strengthened the zloty since mid-February. It was also a recovery of the macroeconomic situation in Germany that provided encouragement for German banks to buy the zloty. At end-February we once again witnessed a weaker zloty, which was partly due to the fact that it is in February (the most difficult month from the point of view of liquidity) when reserves against the NBP are usually settled. The extent of the current account deficit in January published in early February 2000 proved to be no surprise to the participants in the currency market. On the other hand, the interest rate disparity led to a run by foreign investors on treasury bonds in the primary and secondary markets as well as to the appreciation of the zloty. Thus all the records established in the first-half of 1999 were beaten, with the deviation from parity exceeding 4.4%. At end-March, the level of the deviation of the exchange rate from the

Figure 11. Average deviation of market exchange rates from the central exchange rate of US$ and DM/euro, 1997–2000



Source: NBP.
Note: 1997–1998 – DM and from 1999 – euro.

January 1999 parity (over 7.4%) was achieved. The NBP had some problems with eliminating overliquid from the money market although it had sold bonds for 4 billion zlotys. Overliquidity resulted in a fall in short-term interest rates. In the early April 2000 a definite change in the mood set in, and the zloty weakened first of all as a consequence of some comments issued by decision-makers to belie the economic fundamentals of a strong appreciation of the zloty. These opinions were, however, confirmed by a higher-than-expected current account deficit in February 2000. The retreat of foreign investors from the currency market was caused also by the revaluation of IT shares on the Wall Street stockmarket on the black Friday of April 14, 2000.

The full floating of the zloty – this began with the April 12, 2000 with the abandonment of the central exchange

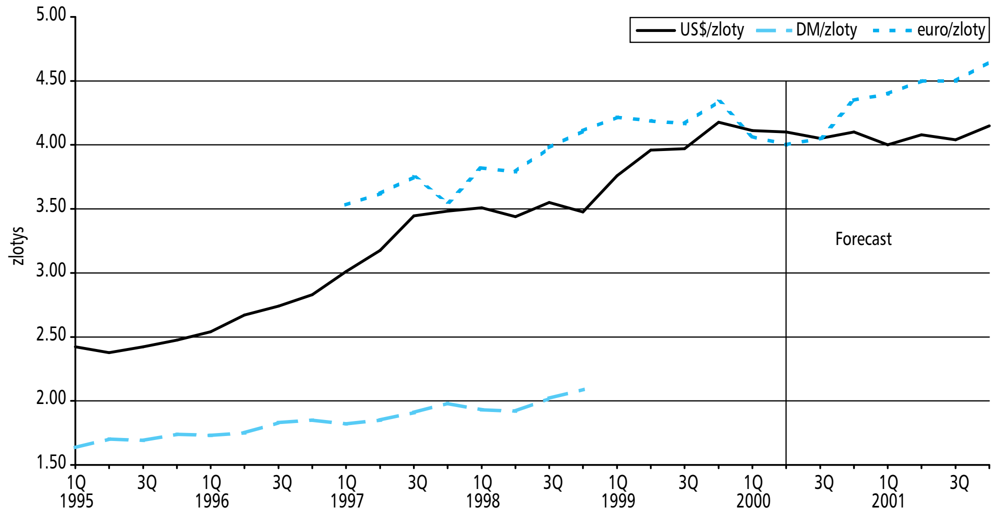
Table 14. Basic exchange rates, 1997–2001 (per zloty)

		US$	DM	ECU/Euro	Real effective exchange rate
1997	1Q-4Q	3.28	1.89	3.71	148.8
1998	1Q-4Q	3.49	1.99	3.92	151.3
1999	1Q-4Q	3.97		4.23	147.2
forecast					
2000	*1Q-4Q*	*4.29*		*4.12*	
2001	*1Q-4Q*	*4.30*		*4.56*	
1997	1Q	3.01	1.82	3.53	150.6
	2Q	3.18	1.85	3.62	149.2
	3Q	3.44	1.91	3.75	146.9
	4Q	3.48	1.98	3.55	144.4
1998	1Q	3.51	1.93	3.82	151.7
	2Q	3.44	1.92	3.79	153.8
	3Q	3.55	2.02	3.98	150.2
	4Q	3.48	2.09	4.11	147.4
1999	1Q	3.76	2.15	4.22	144.5
	2Q	3.96	2.14	4.19	147.4
	3Q	3.97	2.13	4.17	150.1
	4Q	4.18	2.22	4.34	146.7
2000	1Q	4.11	2.08	4.07	158.1
forecast					
2000	*2Q*	*4.35*		*4.00*	
	3Q	*4.40*		*4.10*	
	4Q	*4.30*		*4.30*	
2001	*1Q*	*4.30*		*4.45*	
	2Q	*4.30*		*4.55*	
	3Q	*4.30*		*4.60*	
	4Q	*4.30*		*4.65*	

Source: NBP, real effective exchange rate – JP Morgan, forecasts – CASE.
Notes: 1. Average exchange rates.
2. Real effective exchange rate, 1990 average = 100.

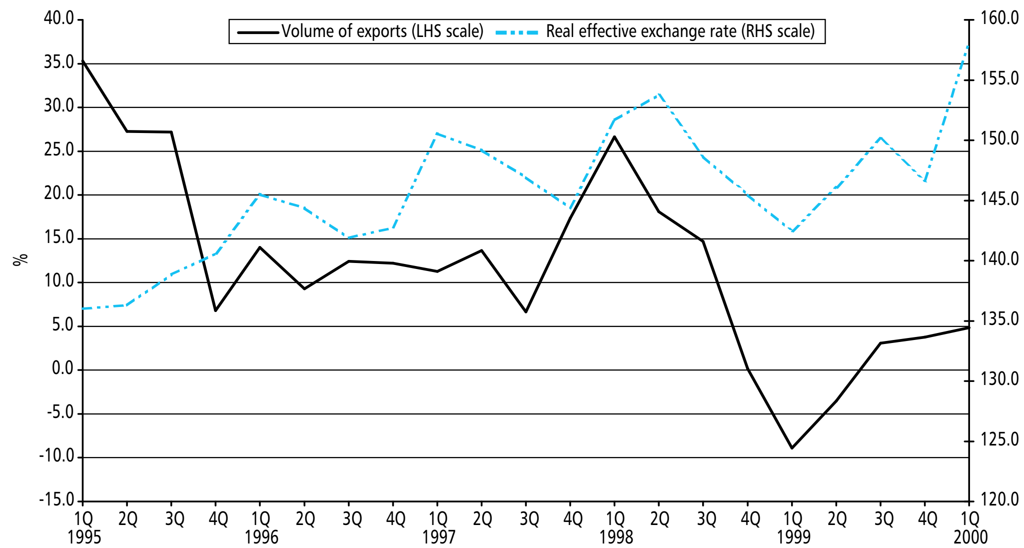
rate and monthly devaluation of the zloty against the euro and dollar basket as well as the elimination of the band of permissible market exchange rate movements – came as some surprise to market participants even though the floating of the zloty had been anticipated since 1999. Lack of a reference point, such as the NBP central parity, became quite a technical problem for the currency market for a few days. An exchange rate risk, even a short-term one, was a real threat to all participants in the market. Trading volume in the currency market following the float-

Figure 12. Basic exchange rates, 1995–2001 (per zloty)



Source: CSO and CASE.
Note: CASE forecast starting from 2Q00.

Figure 13. The volume of exports and real effective exchange rate, 1995–2000 (% change)



Source: CSO and JP Morgan.
Note: Real effective exchange rate (right-hand scale), 1990 average = 100.

ing of the zloty did not exceed US$2 billion, most often fluctuating around US$1.5–1.7. The development of the currency market and its instruments is likely to become the fundamental benefit for the domestic financial market resulting from the floating zloty. The trade volume in the currency market in Poland so far has provided the best evidence of the structural underdevelopment of the currency market and lack of interest in its development on the part of Polish monetary authorities. Now, however, in view of the expected proceeds from privatisation, and due to a series of announcements of a wide ranging sterilisation of foreign currency inflows, the present currency market in Poland may turn out to be too weak and disorientated to hope for its fast growth and development. On the other hand, in the short run a flat currency market may lead to very sharp movements in the zloty exchange rate in the situation when investors start to manifest a herd behaviour. The NBP will probably try to avoid any interference in the currency market as it tends to determine an equilibrium exchange rate and makes a declaration of its interests in medium as well as short-term inflation targets. Possible intervention in the market on the part of the NBP may signify the bank's serious concern about the situation. In this case, this kind of policy will not help to stabilise the market. NBP's operational target seems to increase the number of degrees of freedom in monetary policy both by the policy of eliminating overliquid assets from the money market and by creating freedom of action at both ends of the currency market with the large-scale use of the power of persuasion. Therefore, 1Q00 and the early April 2000 provide a foretaste of the range of movements in the currency market over the whole year 2000, as well as of the variety of factors, not only those of fundamental nature, to affect the zloty exchange rate.

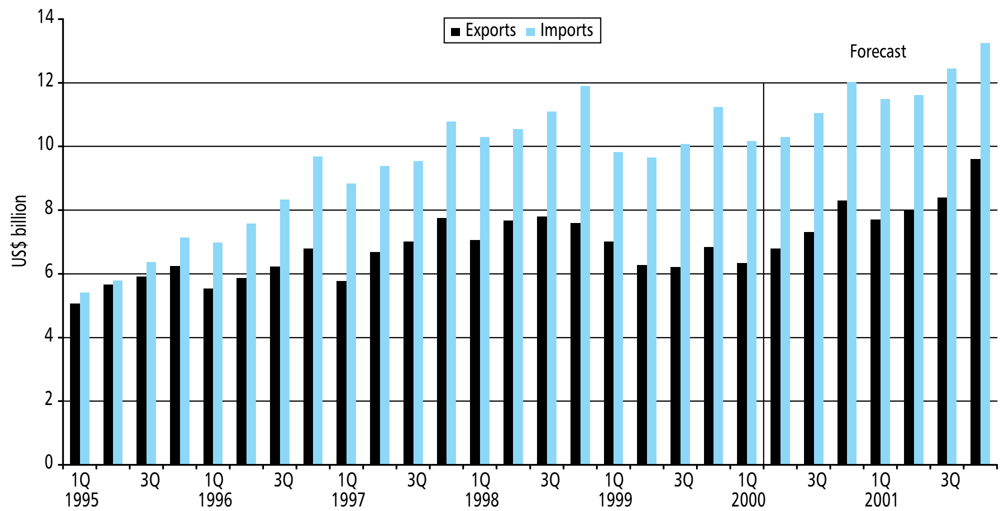
We expect that in 2000 the zloty will be relatively stronger than it was in the previous year (see Table 13). In 2001, the zloty is likely to become weaker (corresponding to the inflation). At the same time, in view of the assumed relative weakening of the dollar against the euro we forecast a stable zloty exchange rate against the dollar and a weaker zloty against the euro.

Foreign trade

- **Stable imports**
- **Continued low exports**
- **Weak euro and structural determinants as the main causes of unsatisfactory exports**
- **Chances of improvement in exports in the second-half of 2000**

According to NBP, imports in 1Q00 amounted to US$10.17 billion, which was US$339 million higher yoy,

Figure 14. Exports and imports, 1995–2001 (US$ billion)



Source: NBP and CASE.
Note: CASE forecast starting from 2Q00.

however it was US$1.14 billion less than in 4Q99. According to our estimates, the volume of imports in 1Q00 increased 7.9% yoy.

The relatively low dynamics of imports is the effect of a restrictive economic policy. Restriction in the budget deficit leads to lower domestic demand, including demand for imported goods. It should be remembered that about 80% of imports consist of investment and intermediate goods. On the other hand, a significant growth in industrial production should lead to faster growth in imports. However, weaker results of exports have weakened this mechanism as the export production is very import-intensive.

In 2000, we forecast a relatively stable level of imports. This will be a continued effect of the restrictive budgetary and monetary policies (at least until end-3Q00). In addition, the growth rate of investment in 2000 will remain at a stable level of about 11%, that is far below that prior to 1999. It is only the faster growth of real households' income that may boost imports.

We would like to draw attention to the structural character of the large volume of imports in Poland. In an transition economy large investments are necessary to ensure fast economic growth. Since the level of domestic savings is low in Poland, investments must be financed by foreign

Table 15. Exports, imports and net exports; 1997–2001 (US$ billion)

		Exports			Imports			Net exports		
		NBP	CSO	National accounts	NBP	CSO	National accounts	NBP	CSO	National accounts
1997	1Q-4Q	27.23	25.75	36.72	38.55	42.31	42.80	-11.32	-16.56	-6.07
1998	1Q-4Q	30.12	28.23	44.62	43.84	47.05	52.92	-13.72	-18.83	-8.30
1999	1Q-4Q	26.34	27.41	39.59	40.79	45.75	50.76	-14.45	-18.34	-11.17
forecast										
2000	*1Q-4Q*	*28.74*	*31.27*	*43.91*	*43.53*	*50.95*	*56.33*	*-14.79*	*-19.68*	*-12.42*
2001	*1Q-4Q*	*33.70*	*36.77*	*50.81*	*48.79*	*58.98*	*65.48*	*-15.09*	*-22.20*	*-14.66*
1997	1Q	5.77	6.12	9.33	8.84	9.77	9.95	-3.07	-3.65	-0.62
	2Q	6.69	6.31	9.06	9.38	10.56	10.51	-2.69	-4.24	-1.45
	3Q	7.02	6.21	8.85	9.55	10.15	10.19	-2.53	-3.94	-1.34
	4Q	7.75	7.11	9.48	10.78	11.84	12.15	-3.03	-4.73	-2.67
1998	1Q	7.06	7.02	10.82	10.30	11.09	12.59	-3.24	-4.06	-1.77
	2Q	7.67	7.04	11.31	10.55	11.70	13.16	-2.88	-4.65	-1.85
	3Q	7.80	6.89	11.13	11.10	12.00	13.09	-3.30	-5.10	-1.96
	4Q	7.60	7.27	11.35	11.90	12.28	14.09	-4.31	-5.00	-2.73
1999	1Q	7.01	6.57	9.92	9.83	10.37	12.64	-2.82	-3.80	-2.71
	2Q	6.27	6.56	9.67	9.64	10.97	12.78	-3.37	-4.41	-3.12
	3Q	6.21	6.75	10.49	10.08	11.49	12.93	-3.87	-4.74	-2.44
	4Q	6.84	7.53	9.52	11.23	12.92	12.41	-4.39	-5.39	-2.89
2000	1Qe	6.34	6.98	10.40	10.17	11.45	13.65	-3.83	-4.47	-3.25
forecast										
2000	*2Q*	*6.80*	*7.30*	*10.61*	*10.30*	*12.17*	*14.27*	*-3.50*	*-4.86*	*-3.66*
	3Q	*7.30*	*7.93*	*11.75*	*11.04*	*13.04*	*14.28*	*-3.74*	*-5.11*	*-2.54*
	4Q	*8.30*	*9.06*	*11.15*	*12.02*	*14.29*	*14.12*	*-3.72*	*-5.23*	*-2.97*
2001	*1Q*	*7.70*	*8.55*	*12.56*	*11.48*	*13.39*	*16.22*	*-3.78*	*-4.83*	*-3.65*
	2Q	*8.00*	*8.66*	*12.34*	*11.62*	*14.20*	*16.55*	*-3.62*	*-5.54*	*-4.21*
	3Q	*8.40*	*9.27*	*13.42*	*12.44*	*15.17*	*16.54*	*-4.04*	*-5.89*	*-3.12*
	4Q	*9.60*	*10.29*	*12.49*	*13.25*	*16.22*	*16.17*	*-3.65*	*-5.93*	*-3.67*

Source: NBP, CSO, estimates for CSO data (e) and forecasts – CASE.
Note: National accounts according to the CSO definition (merchandise trade plus the value of transport, construction and communication services, net processing turnover, printing services and others).

capital. Thus a large inflow of foreign direct investment leads to an increase in imports. Therefore it is not likely that the volume of imports can be significantly reduced, and the trade deficit may be bring down only by increasing exports.

In 1Q00, exports amounted to US$6.33 billion which is worse than in 4Q99 (by US$508 million) and also worse by US$678 yoy. Despite low dynamics of exports in 1Q00, higher exports in March 2000 offer some hope of a recovery of exports in the next few quarters. **We estimate that the export volume increased 6.8% yoy in 1Q00. This result does not seem to be very satisfactory in view of the low base effect – a 7.7% decline in the export volume in 1Q99.**

It should be kept in mind that exports and imports in nominal terms are affected by the dollar exchange rate against the euro, which in 1Q00 fell on average by 13% yoy. About 55% of export payments and nearly 60% of import payments are effected in the currencies of the euro zone. That is why the growth rates of trade volumes in terms of the euro would have been much higher.

No significant changes have been noted in the geographical structure of Polish exports. The share of exports to the EU which amounted to 70.5% of the total exports in 1999 has continued to increase, including the 36.1% share of exports to Germany alone – unchanged since 1998. So far, no clear trend has been observed in Poland's exports to Russia: over the whole year, Russia ranked the 10th (2.6%), the exports to that country amounting only to 45% of the respective dollar-denominated figure of 1998. However, after two months of 2000 Russia fell out of the first ten importers and took the 11th place.

In our opinion, unsatisfactory results of Polish exports stem mainly from the overlapping of the weak euro and structural problems. Over the past decade the trade structure of Polish manufacturing has not substantially changed despite radical geographical re-orientation of foreign trade. Poland has continued to produce and export low value-added and intermediate goods. According to calculations made by K. Marczewski and A. Wysocka the correlation coefficient between the structure of manufacturing and the structure of exports to the EU was 0.21 in 1998, whereas the corresponding coefficient for exports to the Central and Eastern European markets was 0.83. One should also mention that in 1994 the above correlation coefficients were almost identical to the present ones (0.32 and 0.82 respectively).

The income elasticity of imports is higher than the price elasticity. That is why economic recovery in EU countries should offset the negative effects of the weak euro. However, in view of the structure of Polish exports (many semi-finished products and raw materials) the price elasticity should be higher. This is the reason why any weakening of the euro exerts an important influence on the poor results of Polish exports. On the other hand, one should not expect that the short-term policy of a weak zloty can solve Poland's export difficulties since this policy does not provide any solution to the structural determinants underlying the problem of exports.

In our opinion it is the Polish large domestic market that may provide partial explanation why there have been so few structural changes in industry. Since Polish producers are faced with a huge domestic market there seem to be few incentives for them to search for new markets abroad. With dynamic domestic demand plus high inflation in the absence of a currency risk, production for the domestic market has always been more profitable than that for exports. In addition, export goods, especially those to industrialised countries, must meet much more stringent quality standards.

Lack of fast changes in (and insufficient attempts at) modernising segments of Polish industry producing for exports may also stem from the unfavourable structure of the direct foreign investment inflow. According to the PAIZ (the Polish Agency for Foreign Investment) data, 50.8% of all investment inflows to Poland until end-1999 had been placed in sectors other than manufacturing, i.e. in financial services, trade, repairs, construction, transport, etc. Out of the remaining 50%, some 27% had been invested in the production of foodstuffs, drinks and tobacco products, which are consumed in 90% at home. Thus most foreign investment have been placed in the sectors that produce or supply services to the domestic market.

Institutional environment (such as the banking sector, export credits and guarantees) also is of some significance. In view of high internal interest rates Polish manufacturers are at a disadvantage. Again marketing and promotion seem to be often ignored. In this respect, Polish producers must learn a lot to match up to those from industrialised countries. What is also important is that the state should take more action to promote Polish enterprises and businesses by, among other things, facilitating their participation in international trade fairs and exhibitions.

In spite of the above, we feel optimistic about the improvement of Polish exports in the second-half of 2000. Our forecast is based on the significant economic rebound in the EU, especially in Germany, and on the stronger position of the euro. Additionally, the recent high growth of labour productivity may improve the competitiveness of Polish products. Also, with lower domestic demand the manufacturers will be forced to look for new markets abroad.

Balance of payments

- **Large current account deficit**
- **Continued low level of unclassified current transactions and larger deficit in trade in services**
- **Strong inflows of portfolio investment**
- **Deterioration of the structure of foreign capital inflow**

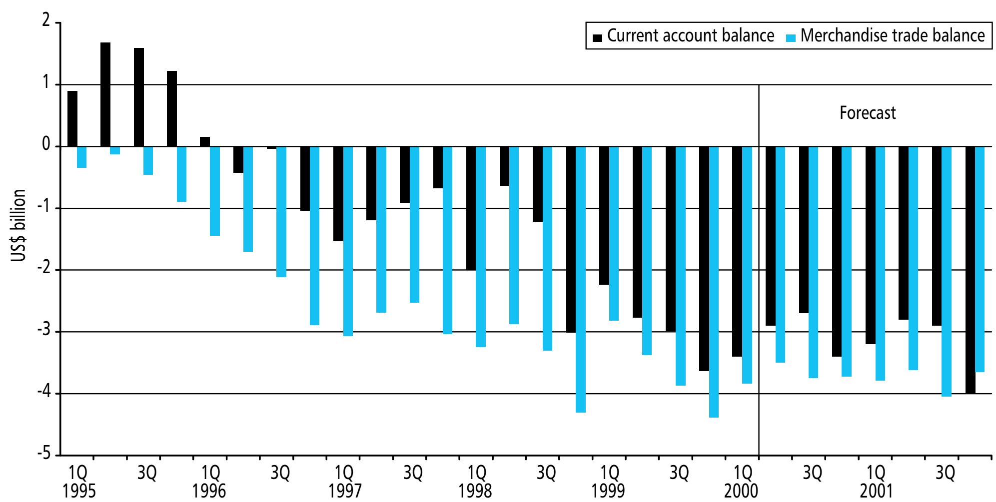
In 1Q00, the current account deficit was US$3.59 billion, which represents a slight improvement on 4Q99 but deterioration of US$1.39 billion yoy. In view of the lower GDP in 1Q00, the deficit as a % of GDP was 9.5%. Seasonal effects may partly account for this situation.

The large current account deficit is a result of the continued relatively large deficit in merchandise trade (US$3.84 billion), low level of the unclassified current transactions (as little as US$729 million), a deteriorating deficit in the trade in services (US$547 million) and, finally, a deficit in revenues (US$295 million) due to debt repayments in March.

The deficit in merchandise trade was US$3.84 billion, which was a significant improvement both on 1Q00 (by US$1 billion) and on 4Q99 (by US$627 million). Unclassified current transactions, after a slight improvement in 3Q99, have continued to remain at a low level, being slightly lower than those at the beginning of 1999. The upward trend in visits by foreigners (especially at the eastern border) in view of the poor result of the unclassified current transactions may reflect structural changes in the cross-border trade. That is why a faster recovery of the transactions of this kind should not be expected. The upward trend in the deficit in the trade of services, which has been noted for almost one-and-a-half year, has led to the record high deficit in Poland's history.

1Q00 saw the largest portfolio capital inflow of US$2.5 billion – US$1.6 billion in March alone. This fact is a result

Figure 15. Merchandise trade balance and current account balance, 1995–2001 (US$ billion)



Source: NBP and CASE.
Note: CASE forecast starting from 2Q00.

Table 16. Components of the balance payments, 1997–2001 (US$ billion)

		Balance on					Net direct investment	Net portfolio investment	Net credits beyond 1 year	Change in foreign currency reserves	Foreign currency reserves
		current account	% of GDP	merchandise trade	unclassified current transactions	capital and financial account					
1997	1Q-4Q	-4.31	-3.01	-11.32	6.01	5.41	3.04	2.10	0.42	2.64	20.67
1998	1Q-4Q	-6.86	-4.36	-13.72	6.00	10.80	4.97	1.33	1.72	6.71	27.38
1999	1Q-4Q	-11.63	-7.54	-14.45	3.64	9.07	6.63	1.08	2.01	-1.89	25.49
forecast											
2000	*1Q-4Q*	*-12.59*	*-7.37*	*-14.80*	*3.88*	*14.27*	*8.72*	*2.60*	*2.85*	*2.10*	*27.59*
2001	*1Q-4Q*	*-12.90*	*-6.67*	*-15.10*	*4.35*	*13.20*	*7.80*	*1.10*	*2.40*	*0.30*	*27.89*
1997	1Q	-1.53	-4.48	-3.07	1.12	1.28	0.46	0.41	0.05	-0.06	17.98
	2Q	-1.19	-3.38	-2.69	1.47	2.36	0.78	1.07	0.17	1.71	19.69
	3Q	-0.91	-2.65	-2.53	1.62	0.80	0.78	0.64	-0.06	0.37	20.05
	4Q	-0.67	-1.73	-3.03	1.80	0.97	1.03	-0.02	0.26	0.62	20.67
1998	1Q	-2.00	-5.71	-3.24	1.16	3.24	1.00	0.21	0.24	2.39	23.06
	2Q	-0.64	-1.65	-2.88	1.72	2.19	1.26	0.36	0.36	2.19	25.26
	3Q	-1.22	-3.10	-3.30	1.87	2.64	1.68	-0.86	0.06	1.83	27.08
	4Q	-3.01	-6.74	-4.31	1.25	2.73	1.02	1.61	1.07	0.30	27.38
1999	1Q	-2.24	-6.30	-2.82	0.80	1.15	1.14	-0.30	-0.11	-0.78	26.60
	2Q	-2.77	-7.50	-3.37	0.79	1.77	1.19	-0.05	0.54	-0.75	25.85
	3Q	-2.99	-7.69	-3.87	1.15	3.28	2.48	-0.08	0.99	0.18	26.03
	4Q	-3.63	-8.55	-4.39	0.90	2.88	1.82	1.52	0.59	-0.54	25.49
2000	1Qe	-3.59	-9.50	-3.84	0.73	3.27	1.52	2.50	0.55	0.10	25.59
forecast											
2000	*2Q*	*-2.90*	*-7.09*	*-3.50*	*0.90*	*3.40*	*2.30*	*0.60*	*0.60*	*0.50*	*26.09*
	3Q	*-2.70*	*-6.24*	*-3.74*	*1.25*	*3.60*	*2.90*	*-0.20*	*0.70*	*0.90*	*26.99*
	4Q	*-3.40*	*-6.95*	*-3.72*	*1.00*	*4.00*	*2.00*	*-0.30*	*1.00*	*0.60*	*27.59*
2001	*1Q*	*-3.20*	*-7.29*	*-3.79*	*0.80*	*3.00*	*1.60*	*-0.10*	*0.80*	*-0.20*	*27.39*
	2Q	*-2.80*	*-6.03*	*-3.62*	*1.00*	*2.80*	*1.70*	*0.20*	*0.70*	*0.00*	*27.39*
	3Q	*-2.90*	*-5.96*	*-4.04*	*1.40*	*3.40*	*2.00*	*0.40*	*0.50*	*0.50*	*27.89*
	4Q	*-4.00*	*-7.39*	*-3.65*	*1.15*	*4.00*	*2.50*	*0.60*	*0.40*	*0.00*	*27.89*

Source: Data and estimates (e) – NBP; forecasts – CASE.

of the decision made by the MPC by end-February 2000 to raise interest rates. In consequence of this decision, the disparity in interest rates between Poland and the industrialised countries as well as Hungary and the Czech Republic has widened. In 1Q00, the net portfolio capital inflows exceeded the inflow of direct investment (US$1.52 billion). Therefore, the structure of financing the current account deficit has deteriorated. In 4Q99 the ratio of the portfolio capital to direct investment was 0.8, whereas that in 1Q00 was 1.65.

The NBP policy of non-intervention in the exchange market and the change in the currency structure of the NBP assets have led to only slightly higher foreign currency reserves from US$25.5 billion by end-1999 to US$25.6 billion by end-March 2000.

We forecast that the current account deficit will stabilise at a slightly lower level. This will be possible due to the expected recovery of exports and moderate growth of imports. Over the whole year, in 2000 the current account deficit to GDP will amount to 7.4%. By end-2000, the reserves are likely to rise to US$27.6 billion, which be still sufficient to cover the average 11-month imports.

Public finances

- **Tighter fiscal policy**
- **Improvement in the financial standing of ZUS and Regional Health Funds**

Tightening of fiscal policy in 2000 is a fundamental condition to reduce inflation and the current account deficit. Easier fiscal policy in 1999 was applied mostly to the public finances sectors outside the government budget. This was the reason why the analysis of the available results of the budget in 1Q00 is only of limited value in estimating the effect of fiscal policy on other sectors of economy. What is of relatively greater importance is the analysis of the process of implementation of the programme to redress the situation in ZUS and the financial aspects of the operation of Regional Health Funds. The situation in the local government sphere should also be monitored.

Following 1Q00, the budget deficit stood at 45% of the projected value (see also Table 17), which should not give any reason for worry since the above deficit has stemmed from the concentration of some expenditures (especially subsidies to the local governments) in the first few months of 2000. In addition, in March the yearly premiums (the so-called "13th salary") to employees and interests to the members of the Paris Club had to be paid out.

In 1Q00, the structure of budgetary revenues changed compared to previous year: the growth rate of corporate income tax revenues was higher, whereas the growth rate of personal income tax revenues was lower than the total growth of budget revenues. It should be emphasised that despite accelerated inflation, rise in crude oil prices and additional rises in the excise tax, the returns from indirect taxation have grown at a faster rate than total revenues. In 2000, no payments were obtained from the NBP profit. Until then the deficit was financed from the 9 billion zlotys which the government had placed with the NBP at the beginning of the year. The above sum included 4.1 billion zlotys from the previous year's assets and 3 billion zlotys from the January privatisation proceeds.

The implementation of the 2000 budget should prove easier than that of the 1999 budget, primarily because of the lower inflation level adopted in the Budget Act. An additional fiscal impetus to boost domestic demand (although not as big as the difficulties encountered by ZUS in 1999) will come from the implementation of the programme of compensation payments by end-March to old-age pensioners and employees in the government sector. This programme will cover some 900 thousand people entitled to it, the total sum of payments reaching 3.4 billion zlotys.

The health care reform is beginning to bring about good results. Gradual privatisation of the reform will make it possible to introduce sharper competition among health care providers, their number being on the increase with the same number of services provided. A fall in employment is another positive effect of the reform.

By privatising health care local governments will be deprived of direct responsibility and control over the basic health care establishments. In the absence of privatisation, local governments are not only responsible for very costly investment, but also for liabilities incurred by these establishments.

Regional Health Funds, which had their budget credits to the amount of 0.8 billion zlotys written off, have also managed to negotiate favourable interests on the credit of 1 billion zlotys granted to cover the deficit incurred in 1999 as a result of ZUS's failure to transfer some of the insurance contributions to the Regional Health Funds.

The small deficit in local government budget in 1999 stemmed from a fall in the share of investment to 13% of all spending compared with 23% in 1998 (data from the Centre of Regional Studies [CBR]). The above volume of investment may prove to be insufficient to have regional backward development reduced. It may also be inadequate to meet the requirements imposed on co-financing of joint structural EU projects. The authorities in the largest Polish towns are planning their 2000 deficits at 1.3 billion zlotys (0.2% of GDP).

The successful collection of annual settlement declarations by ZUS, associated with paying the defaulted 1999 premiums by some payers, is the best proof that ZUS's efficiency of operation has improved. By end-year, ZUS should be able to put into practice the scheme of individual accounts of the insured.

Thanks to its high revenues, ZUS was able to repay some of its commercial debts. What is more, the more flexible debt management against commercial banks is

Table 17. Selected items of the government budget, 1997–2001 (US$ billion)

		Revenues		Expenditures	Central government balance	
		total	of which tax revenues		zlotych billion	% of GDP
1997	1Q-4Q	119.8	98.5	125.7	-5.9	-1.3
1998	1Q-4Q	126.5	113.8	139.8	-13.3	-2.4
1999	1Q-4Q	125.9	112.7	138.5	-12.6	-2.1
forecast						
2000	*1Q-4Q*	*142.5*	*127.7*	*154.9*	*-12.5*	*-1.8*
2001	*1Q-4Q*	*157.3*	*141.3*	*171.0*	*13.7*	*-1.7*
1997	1Q	23.5	20.2	27.4	-3.9	-3.8
	2Q	27.1	21.1	30.6	-3.5	-3.1
	3Q	32.8	26.4	31.4	1.4	1.1
	4Q	36.4	30.7	36.3	0.1	0.1
1998	1Q	28.7	25.6	32.3	-3.5	-2.9
	2Q	29.3	26.3	35.1	-5.8	-4.4
	3Q	33.1	29.9	34.1	-1.1	-0.8
	4Q	35.5	32.1	38.3	-2.8	-1.8
1999	1Q	27.7	24.8	36.5	-8.7	-6.5
	2Q	28.8	25.2	31.4	-2.6	-1.8
	3Q	32.4	29.5	32.4	0.0	0.0
	4Q	36.9	33.1	38.2	-1.3	-0.7
2000	1Q	31.0	27.7	38.0	-6.9	-4.5
forecast						
2000	*2Q*	*32.8*	*28.9*	*36.9*	*-4.1*	*-2.4*
	3Q	*37.2*	*33.7*	*36.7*	*0.5*	*0.3*
	4Q	*41.5*	*37.4*	*43.4*	*-1.9*	*-1.0*
2001	*1Q*	*34.5*	*30.9*	*42.7*	*-8.3*	*-4.7*
	2Q	*36.3*	*32.1*	*41.2*	*-4.8*	*-2.5*
	3Q	*41.2*	*37.4*	*40.0*	*1.2*	*0.6*
	4Q	*45.3*	*40.9*	*47.0*	*-1.7*	*-0.8*

Source: Data – Ministry of Finance, forecasts – CASE.

likely to make it possible to reduce the cost of servicing debts; the ZUS policy is to borrow money only when it has immediate problems in paying benefits, and to reduces its debt when contributions are paid in. The financial situation in ZUS in 2000 will continue to be difficult, but better management and higher base for calculating premiums, as a result of inflation by end-1999, will probably contribute to relative financial stabilisation.

Essential changes in the management of privatisation proceeds has been brought about by the amended Act on commercialisation and privatisation of state-run enterprises. The government's special foreign account with the NBP to accommodate some 20% of privatisation proceeds has not yet been made use of, although in the first two months of 2000 3.2 billion zlotys were gained out of the projected 20.1 billion zlotys for 2000, mostly due to the sale of the shares of TP SA, KGHM, PZU and crude oil refinery. The projected privatisation proceeds are likely to be exceeded also in 2000.

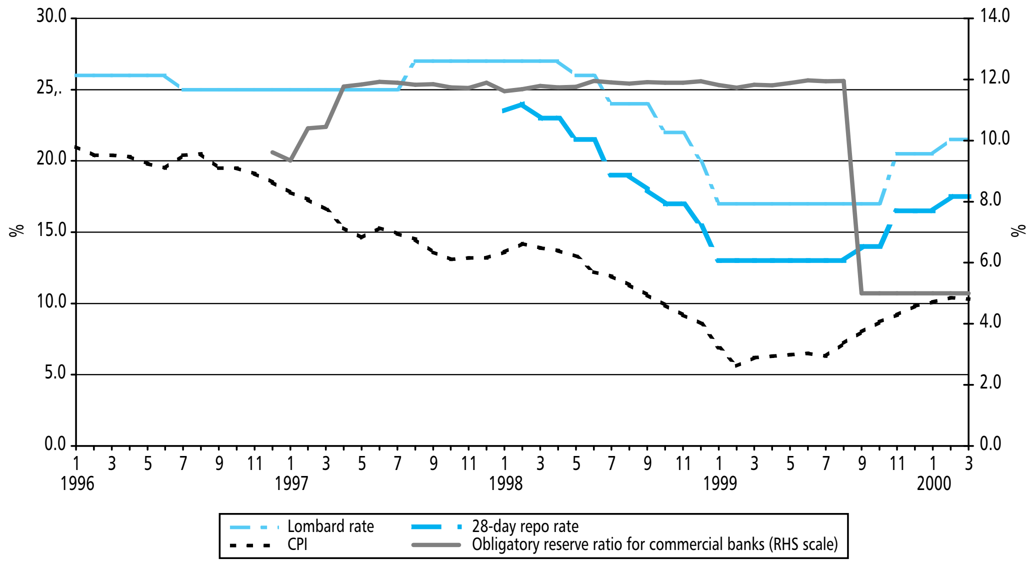
The expected improvement in public finances (see forecast in Table 18) makes it possible to achieve more radical cuts in taxation. The reform of corporate taxes aimed at limiting transfers of profits from Poland is continuing, however the reform of taxes from individuals has still met with controversial opinions. The difficulties concern not only the amount of reduction in tax rates, but also the problem of tax allowances on construction, repairs and family expenditures, as well as the effect of the tax reform on local government budgets. However, the chances that a consensus can be reached with the ruling coalition and the support obtained from the Office of the President are significantly higher than in 1999.

Monetary policy

- **Tightening of monetary policy**
- **Limiting of the overliquidity of the banking sector and decline in money supply**
- **Monitoring of short-term flows**

After 1999 which registered a record fall in the propensity to save and a decline in the growth rate of household credits, 1Q00 saw a radical tightening of monetary and budget policies. As a result of two rises in the NBP interest rates within the span of three months by a total of 450 base points, credit interest rates in commercial banks have gone up by about 100 base points over deposit interest rates. The NBP's policy is still to try to check the scope of granting credits to households. The condition *sine qua non* to achieve this target is to elimi-

Figure 16. Monetary policy instruments, 1996–2000



Source: NBP and CASE.

nate the overliquidity of the banking sector. The next instalment on the debt in foreign currency is due to be paid in September, which means that either the government's special foreign currency account will remain unused and the privatisation process will lag behind, or NBP's active monetary policy instruments will have to be blocked in order to have the assets in this account sterilised. In this way, the possibility of controlling the liquidity in the money market fin the case of short-term flows may be considerably restricted. This situation will lead to sharp movements in both the zloty exchange rate and in short- and medium-term interest rates. The NBP being fully aware of this threat has made more stringent the requirements to obtain reports from commercial banks, especially when the positions of non-residents and currency positions have to be determined.

The two rises in interest rates were due to the need to adjust to inflation growth. If the annual inflation rate continues to remain at the level higher than 10% (to July 2000) the NBP will not be able to reduce its interest rates until end-3Q00. However, the main underlying causes of inflation are those involving costs. If the real interest rates are maintained at a level higher that 8% and the disparity remains higher than 1100 base points against interest rates in industrialised countries, the upward trend in GDP growth and the appreciation of the zloty, may force rather than encourage Polish enterprises to incur short-term foreign credits or those denominated in foreign currencies.

Reserve money and monetary policy instruments

The fall in reserve money by 14.4% in 1Q00 stemmed again from the fall in the budget liabilities against the NBP and from the absence of significant privatisation proceeds. This in turn led to a decline in domestic credits and in a marginal increase in net foreign assets of the central bank. However, foreign debt was due to be repaid in March 2000, which, in view of small privatisation proceeds, meant that the higher deficit had to be covered by rev-

Table 18. Components of the reserve money supply, 1997–2000 (cumulative % change)

		Reserve money (RM)	Net foreign assets (NFA)	Net domestic assets (NDA)	Net claims on government (NCG)	Claims on deposit money banks (CDMB)	Other items net (OIN)
1997	1Q	10.12	5.82	12.05	14.22	-2.17	-7.75
	2Q	20.44	30.20	5.66	26.67	-21.01	-15.43
	3Q	31.65	43.47	11.55	25.77	-14.21	-23.38
	4Q	23.50	57.60	54.16	17.14	37.01	-88.27
1998	1Q	4.82	25.37	-7.00	-5.31	-1.69	-13.55
	2Q	17.54	36.32	-10.22	-8.74	-1.48	-8.56
	3Q	17.50	48.85	-4.39	-6.35	1.96	-26.94
	4Q	26.78	63.44	-0.90	2.95	-3.85	-35.75
1999	1Q	0.44	-0.78	-0.57	-0.50	-0.07	1.79
	2Q	10.20	14.07	1.54	2.10	-0.57	-5.42
	3Q	-13.94	6.15	-3.65	-2.79	-0.87	-16.45
	4Q	-1.57	18.50	-4.75	-3.71	-1.04	-15.34
2000	1Q	-14.44	1.01	-0.98	-1.57	0.60	-14.47

Source: The NBP Bulletin and authors' calculations.

Notes: 1. The shares of components of reserve money are calculated using the following formula: $\Delta RM/RM_{-1} = \Delta NFA/RM_{-1} + \Delta NCG/RM_{-1} + \Delta CDMB/RM_{-1} + \Delta OIN/RM_{-1}$, cumulative in the current year. Net foreign assets were re-estimated (valuation adjustment) using the average exchange rate of the currency basket for a given period to account for fluctuations in the exchange rate of the zloty.

2. Changes in comparison to PEO 1/99 stem from the introduction of the currency basket into calculations instead of using USD/PLN exchange rate.

enues from newly issued bonds the price of which were thus made to fall in the primary market in early February.

Since the beginning of 2000, the market was dominated by pressures to increase interest rates of short- and medium-term monetary policy instruments. In addition to fundamental causes (inflation in excess of 10%) the pressures stemmed from the demand for treasury instruments, actively present in the primary market also by foreign investors and problems involving liquidity of the banking sector in clearing reserves specially in February, the most difficult month in this respect. In February 2000, daily rates of one-day deposits exceeded 20% , which was higher than the respective values of July 1997. By end-March the banks fearing that the situation of January-February may repeat collected assets and thus caused overliquidity in the money market, which led to a reduction in one-day deposits to 5% (on March 30). The NBP reduced the market liquidity by selling 4 billion worth of bonds on March 23. As a result, the rates of monthly deposits failed to fall below 18%, that is above the NBP intervention rate fixed at 17.5% after the rise on February 23, 2000. The rise in NBP interest rates by 100 base points in 1Q00 (predicted in the previous issue of PEO) had resulted from the prospects of the continued annual inflation rate at a level higher than 10% and from the demand for credits (see The banking system and broad money). As a consequence of the anticipated rise in interest rates, and the subsequent rise in their disparity, the inflow of a short-term capital has increased considerably and thus the zloty has strengthened since half-February (see Exchange rate). In 1Q00, liquid foreign currency reserves increased by only US$145 million despite the inflow of US$1–2 billion to the banking system. All this stemmed from the appreciation of the zloty, NBP sterilisation and the continued current account deficit at a level above US$1 billion monthly.

The banking system and broad money

Tightening of the monetary policy and efficient elimination by the NBP of overliquidity in the monetary market

Table 19. Components of broad money, 1997–2000 (cumulative %)

		Broad money (M2)	Net foreign assets (NFA)	Net domestic assets (NDA)	Net claims on government (NCG)	Claims on private sector (CPS)	Other items net (OIN)
1997	1Q	5.04	-0.06	8.20	2.29	5.91	-3.10
	2Q	12.59	6.02	12.89	2.17	10.72	-6.33
	3Q	20.38	10.91	18.10	1.66	16.43	-8.63
	4Q	30.89	15.20	27.18	6.28	20.90	-11.49
1998	1Q	2.25	3.76	0.85	-2.85	3.70	-2.36
	2Q	8.97	4.79	5.25	-2.60	7.86	-1.08
	3Q	15.35	4.33	13.76	0.86	12.90	-2.74
	4Q	25.12	9.72	20.60	3.42	17.18	-5.20
1999	1Q	4.30	-0.53	5.74	1.18	4.55	-0.91
	2Q	7.01	2.35	9.59	1.77	7.82	-4.93
	3Q	11.42	2.45	13.19	0.14	13.06	-4.23
	4Q	19.36	6.43	18.45	1.51	16.94	-5.53
2000	1Q	-0.67	2.01	-0.64	-3.62	2.98	-2.04

Source: The NBP Bulletin and authors' calculations.

Notes: 1. The share of broad money components are calculated using the following formula: $\Delta M2/M2_{-1} = \Delta NFA/M2_{-1} + \Delta NCG/M2_{-1} + \Delta CDMB/M2_{-1} + \Delta OIN/M2_{-1}$, cumulative in the current year. Net foreign assets were re-estimated (valuation adjustment) using the average exchange rate of the currency basket for a give period to account for fluctuations of the exchange rate of the zloty.

2. Changes in comparison to PEO 1/99 stem from the introduction of the currency basket into calculations instead of using USD/PLN exchange rate.

Table 20. Calendar of the most important events in the monetary policy of the NBP over the period 3Q99–1Q00

Source	Date of the resolution	Events
J. NBP No. 15	21 July, 1999	Rate of reserve requirement on banks deposits cut and unified at the level of 5% beginning from august 30
J. NBP No. 19	22 September, 1999	28-day repo rate at least 14%
P.M. No. 32	22 September, 1999	Announcement of monetary policy guidelines for 2000
J. NBP No. 20	17 November, 1999	NBP rediscount rate 19% Lombard rate 20.5% Refinancing rate 20.5/21.5% 28-day repo rate at least 16.5%
J. NBP No. 21	19 November, 1999	Interest rate on NBP current deposits 6.15%
J. NBP No. 26	22 December, 1999	Amendment to the law on reserves due to bank insurance, in force on 30 March, 2000
J NBP No. 1	23 February, 2000	NBP rediscount rate 20% Lombard rate 21.5% Refinancing rate 21.5/22.5% 28-day repo rate at least 17.5%
J NBP No. 2	25 February, 2000	Interest rate on NBP current deposits 6,45%
J NBP No. 4	10 March, 2000	A change in the standard of statistics that are reported by commercial banks

Source: Official Journal of the NBP, various issues. Authors' compilation.

has led for the first time to a decline in broad money supply in 1Q00. This decline came as a result of a fall in the budget debt since January 2000 by as much as 11.9% and 14.7% by end-March, as well as of the growth of foreign currency deposits by individuals (by 8.2% since the beginning of 2000) and those by corporations (by 24.9%). However, the growth rates of deposits by individuals have registered the month-on-month decrease: they amounted to 4.1%, 2.4% and 1.5% in January, February and March, respectively. Over the same period, zloty-denominated deposits by corporations have also seen a sharp fall: 14.5% in January and 15.8% over the whole 1Q00 as a result of a rapid rise in December 1999 following the arrest of payments by banks. Nevertheless, the growth rates of credits for enterprises have also notched up a decrease: 2.5%, 10% and 0.9% in January, February and March, which has been quite a sensational event in the monetary policy in recent years. The growth of deposits and lower credit expansion can be attributed to the rise in interest rates in November 1999. Commercial banks have introduced higher interest rates on credits than on deposits with a two or three- month delay following the official rise in November. It seems, therefore, that it was only the threat of a new rise in rates and then its implementation in February that caused the disparity between the rates to the disadvantage of borrowers.

Net foreign assets in the banking sector increased US$1.3 until end-March. The rise occurred particularly in February and March 2000, which, with the growth of foreign portfolio investment since February 2000, means that it was the disparity of interest rates following the hike in NBP rates in that month that had a decisive effect on the higher volume of assets. The broad money velocity and domestic money velocity continued at a stable level (2.4 and 2.9 respectively), but the M1 money velocity dramatically fell to 5.4, whereas in the previous years it remained stable at a level of 7.6–8.3.

We expect the trends observed in the money market in 1Q00 to continue through end-2000. As a result, we forecast a decrease in the growth rate of consumption credits from over 51% to 23% in 4Q00. In 2001, after reductions in interest rates credit expansion is likely to accelerate again to about 27%, respectively. Credits for enterprises will also register a slower rate of growth (more than 20% and 18% in 2000 and 2001, respectively). At the same time, high interest rates may lead to higher zloty-denominated deposits by 35 and 40 billion zlotys, respectively. A detailed analysis of the fundamental components of assets and liabilities in the banking sector is given in Appendix 11.

Center for Social and Economic Research

Changes in Poland's balance of payments structure on entering the European Union (simulation for the years 2000-2014)

This report presents some selected results of our studies aimed at outlining the most important trends in Poland's economic development in 2000–2014, with special emphasis on the changes in the Polish balance of payments on entering the European Union (EU). The studies were based on simulation analyses with the use of an aggregated growth model (the CGE general balance model) on the one hand, and on the employment of a specially designed detailed balance of payments model related to national calculations generated by the CGE model. In the studies we have also made wide use of the method of international comparisons, first of all that of comparing Poland's situation with that of Spain, Portugal and Greece at the time of their entry into the EU.

The problem to which we have devoted special attention was that of the risk of a currency crisis occurring in Poland in 2000–2014. This risk may be expected to disappear completely only after Poland has joined the Euro zone. Several factors such as cumulation of economic balance prior to entering the EU, resulting from the agreements with the Paris and London Clubs, high debt repayments in 2004–2008 as well as the efforts to meet the Maastricht criteria of nominal convergence, implemented in a more or less consistent and careful way, can altogether significantly affect the foreign currency risk.

Our projection takes into account the probable effects of Poland's membership in the EU from 2004. Some earlier membership (e.g. in 2003) cannot of course be excluded or that at a more distant future (2007–2008). What Poland's membership in the EU means is, among other things, accelerated economic growth (at least temporarily), rising incomes, stronger domestic currency, intensive inflow of union's transfers intended to develop infrastructure. On the other hand, it also means that the competition pressures involved in full liberalisation and implementation of the principles of acquis communautaires, and the more aggressive market strategy pursued by international corporations will considerably be exacerbated. In other words, the adopted pathway for Poland's entry into the EU strongly affects the results of the macroeconomic and balance of payments projections.

When determining the trends in Polish economic development for 2000–2014 we made an assumption of a continued high growth of domestic absorption especially high growth of investment backed up by inflows of foreign investment and growing efforts by Polish enterprises to modernise, imposed by stronger competition pressures. A relatively positive and even improved image of Poland will undoubtedly be more attractive to foreign direct investment (FDI).

According to our projections, a downward trend in economic growth in 1998-1999 will be only temporary. Once the external shock has been overcome, in 2000–2014 the economy will register an upward trend in GDP of 5–6%, with domestic consumption rising at slightly less than 5%, and investments growing at about 10% annually. Both the growth rates of imports and exports are likely to be relatively high, i.e. of about 10%. As a result, the current account deficit in GDP will be hovering around 5%, which should provide protection against a potential currency crisis.

After having joined the EU Poland will see a several-year-long growth of investment (11–12%) and a consumption of 6%. The growth of imports will exceed that of exports (accelerated to about 15% and 13% respectively). As a result, GDP growth will accelerate temporarily to 6.5%. The trade balance in the balance of payment will significantly deteriorate (by 2 percentage points of GDP). At the same time, the increased EU transfers will help to maintain the current account balance at 5% of GDP.

In order to test and analyse the likely changes in the balance of payments structure, involving the changes in the risk of a currency crisis, we have carried out three simulation experiments that differ in respect of the economic policy pursued by Poland. Here are the respective scenarios:

- *a baseline scenario* involving in principle the continuation of the present economic policy aimed at gradual reduction of the public sector deficit, gradual disinflation and entry into the EU zone in 2007,
- *a fiscal irresponsibility scenario* which assumes that, instead of being balanced, consumption spending pressures will drive the deficit to about 4% of GDP, and the efforts to meet the Maastricht convergence criteria will not be taken until 2008–2010,
- *a balanced exchange rate scenario* which assumes that Poland will pursue a policy of cautious foreign currency exchange with the aim of maintaining the current account deficit at about 6% of GDP in 2000–2004, that is until Poland joins the EU, the compliance with the Maastricht convergence criteria being only possible by adequate adjustment of its fiscal and monetary policies.

It should be noted that none of the above scenarios seems to be extreme; even that of 'fiscal irresponsibility' does not lead to a crash in public finances.

The most important changes in Poland's balance of payments in the baseline scenario are shown in Figure 17 (the trend in changes is similar in all three scenarios). These are

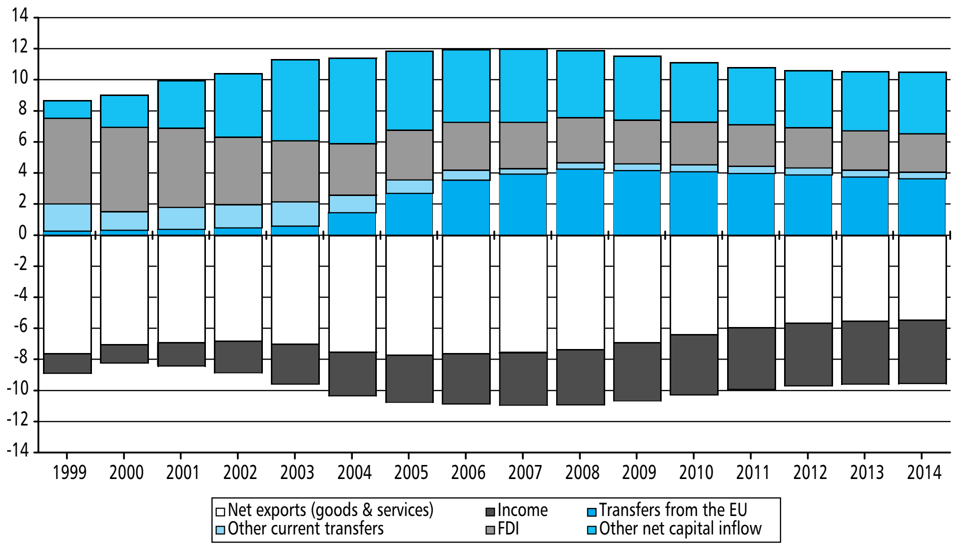
(a) after the long period of FDI inflows in 1999–2002 (as a result inter alia of privatisation proceeds) slight downward trend is expected, followed by a stable inflow of FDI and other forms of capital since the latter must fill up the gap stemming from lower DFI inflows in 2003–2005,

(b) the EU transfers in 2005–2008 will gain in importance significantly,

(c) new and strong foreign currency outflows due to income (interests and profits transferred abroad), which from 2007 on are likely to exceed the volume of direct investment inflows,

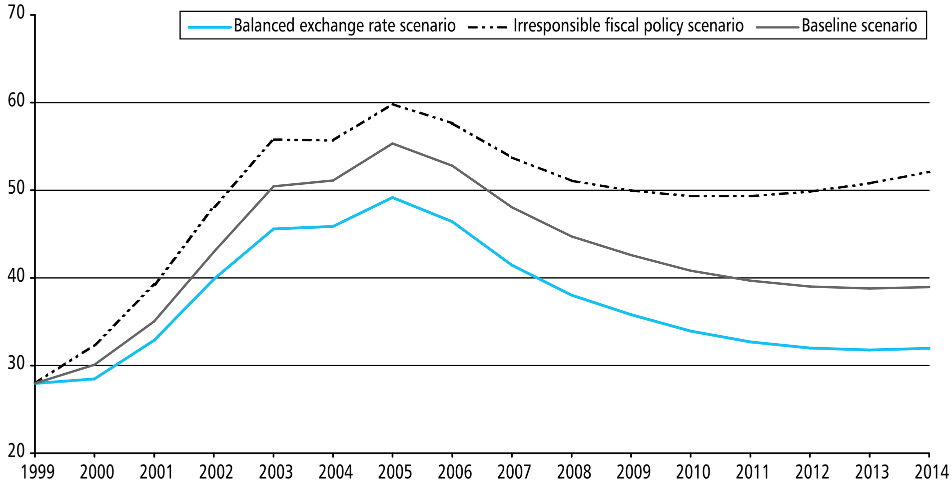
(d) gradual deterioration in trade balance, especially in 2004–2007, and its subsequent fall as a percentage of GDP.

Figure 17. The structure of Poland's balance of payment according to the baseline scenario, 1999–2014 (% of GDP)



Source: Authors' calculations.

Figure 18. The share of short-term and portfolio capital in the total amount of Poland's debt (in simulation experiments), 1999–2014 (%)



Source: Authors' calculations.

Having joined the EU, Poland will remain an importer of capital, however from 2008–2009 on the relative volume of the import of capital will gradually decrease, and the EU transfers will provide one third of all assets imported by Poland.

In our simulation calculations we have also analysed the risk of a currency crisis, using a number of relevant indexes. Figure 18 shows one of the indexes which are most closely related to the risk of currency crisis, that is the share of short-term credits and portfolio capital in the total amount of Poland's foreign debt. The higher is this share (and also the index) the most likely become the prospects of serious exchange perturbations, as the portfolio and short-term capital can then easily leave Poland.

The most important conclusions drawn from our simulation studies are

(a) the threat of a foreign currency crisis will definitely increase in 2000–2004, that is until Poland joins the EU,

(b) the peak in the short-term capital share in the debt will occur in 2004–2006, then the above mentioned index will subsequently fall,

(c) rational macroeconomic policy (either according to the baseline or balanced exchange rate scenarios) leads to a considerable fall in the above index, and, consequently, lessens the risk of a crisis.

It should be noted that in both scenarios of a rational economic policy the risk of a crisis rapidly diminishes after 2005, and in 2007–2009 (after Poland joins the currency union) it disappears altogether. In the fiscal irresponsibility scenario the threat of a crisis does not disappear at any time, and in 2012–2014 it may be even slightly greater.

The general conclusion drawn from our studies is that Poland's membership in the UE will result in serious changes in the Polish balance of payments. These changes will make it possible to have a high GDP growth maintained. Nothing will, however, free Poland from the obligation to pursue a prudential economic policy. Inconsistent policy may be expected to lead to serious perturbations or even to a currency crisis.

Threats

1. The greatest threat to the Polish economy in 2000 is and will be the high current account deficit whose further increase may lead to a currency crisis in a situation of massive outflows of portfolio capital and radical declines in inflows of foreign direct investment.

2. Low propensity to save and high interest rates encourage Polish manufacturers to incur debt abroad. If the demand for foreign short-term credits increases, the risk of a currency crisis will undoubtedly become greater.

3. The weaker euro (to less than US$0.9) coupled with the unfavourable structure of the Polish industry may, to a large degree, reduce the growth of Polish exports to the EU markets.

4. High unemployment may result in excessive falls in domestic demand.

5. The Polish economy could be affected by an eventual crash of the world's largest stock exchanges. This could lead to lower exports of capital world-wide as well as further rises in interest rates in industrialized countries. As a result, outflows of portfolio capital may start to occur and the inflows of foreign investment may dry up. As a consequence, the zloty may weaken considerably and in turn may spur inflation.

6. In 2000, weaker tensions in the general government budget can be expected compared with 1999. However, larger-than-expected privatisation proceeds may give way to a temptation of pursuing a less restrictive budget policy, especially in 2001. As a consequence, domestic demand may grow excessively, which would lead to general macroeconomic instability.

Recommendations for economic policy

1. In 2000, a restrictive budget policy combined with properly adjusted levels of real interest rates (lower than the present ones) would constitute the best policy-mix. The Monetary Policy Council should lower interest rates when inflation drops, however it should not necessarily increase rates when inflation rises.

2. It will be possible to have interest rates lowered when the Polish economy becomes stable, and inflationary pressures (in terms of both CPI and the current account) start to decrease.

3. It the current account deficit continues to rise in 2Q00, public consumption and the transfers from the budget directly leading to the growth of domestic demand should be temporarily reduced.

4. In the case of the continued weak euro, economic policy should aim at reducing domestic demand growth rather than at artificially boosting exports.

5. Long-term economic policy should aim at reducing income taxes, which will make possible increases in domestic savings and investment as well as in labour demand. As a result, unemployment will likely fall.

6. The uncertain situation in the general government budget requires tighter fiscal discipline and an avoidance of any additional financing of deficits in para-budgets (e.g. ZUS) from privatisation proceeds.

Appendix

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Table A1. GDP in 1998 prices, 1994–2001 (% change yoy)

		GDP	Gross value-added					
			total	agriculture and forestry	manufacturing, mining, etc.	construction	market services	non-market services
1994	1Q-4Q	5.2	4.9	-15.1	9.6	2.7	6.9	7.4
1995	1Q-4Q	7.0	6.7	10.4	10.2	5.8	6.0	2.5
1996	1Q-4Q	6.0	5.3	2.5	7.6	2.8	5.3	2.6
1997	1Q-4Q	6.9	6.5	1.2	10.3	13.6	4.4	3.0
1998	1Q-4Q	4.8	4.7	5.8	4.3	9.1	4.8	1.9
1999e1	1Q-4Q	4.1	3.8	0.3	4.7	3.8	4.6	1.3
forecast								
2000	*1Q-4Q*	*5.4*	*5.2*	*3.8*	*7.7*	*5.6*	*4.7*	*1.6*
2001	*1Q-4Q*	*6.3*	*6.1*	*2.8*	*8.9*	*10.0*	*5.1*	*2.0*
1995	1Q	6.2	6.6	7.3	11.1	7.0	4.6	4.4
	2Q	6.7	6.7	8.1	10.6	7.3	5.1	3.8
	3Q	8.1	7.4	16.3	9.9	6.1	6.0	3.2
	4Q	6.8	6.1	9.0	9.3	4.1	6.8	-0.3
1996	1Q	3.4	2.4	-2.0	6.1	-18.5	3.2	2.4
	2Q	5.5	4.4	2.2	6.9	-4.1	5.2	1.8
	3Q	7.2	6.5	2.7	9.8	4.9	6.2	2.9
	4Q	7.9	7.7	6.7	7.6	21.9	6.6	3.4
1997	1Q	6.9	6.4	-1.5	8.7	14.7	5.5	4.7
	2Q	7.5	6.7	1.7	11.5	15.6	4.4	1.8
	3Q	6.7	6.4	3.2	10.7	13.3	4.2	0.7
	4Q	6.4	6.3	0.3	10.2	12.2	3.7	4.0
1998	1Q	6.5	6.4	0.8	10.5	14.7	4.2	3.4
	2Q	5.3	5.2	4.5	5.4	10.9	5.6	-0.2
	3Q	4.9	4.8	5.3	3.4	8.8	5.9	1.2
	4Q	2.9	2.8	12.9	-1.1	6.1	3.6	2.6
1999e1	1Q	1.6	1.4	1.3	-2.7	2.1	4.2	0.9
	2Q	3.0	2.8	-0.6	1.6	3.2	4.3	1.0
	3Q	5.0	4.7	0.0	7.5	3.6	4.8	2.7
	4Q	6.2	5.9	0.9	11.5	5.1	4.9	0.9
2000	1Qe2	6.0	5.7	1.4	10.8	4.4	4.7	1.3
forecast								
2000	*2Q*	*5.0*	*4.7*	*1.5*	*7.5*	*4.0*	*4.4*	*1.5*
	3Q	*4.9*	*4.7*	*4.0*	*5.8*	*5.5*	*4.6*	*1.8*
	4Q	*5.7*	*5.5*	*8.0*	*7.0*	*7.0*	*5.0*	*1.8*
2001	*1Q*	*5.9*	*5.7*	*5.0*	*8.4*	*8.7*	*5.0*	*1.6*
	2Q	*6.6*	*6.4*	*4.0*	*10.2*	*9.1*	*5.1*	*2.0*
	3Q	*6.1*	*5.9*	*2.0*	*8.0*	*9.8*	*5.2*	*2.1*
	4Q	*6.5*	*6.3*	*1.0*	*9.0*	*11.2*	*5.1*	*2.2*

Source: Data and estimates (e1) – CSO; estimates (e2) and forecasts – CASE.
Notes: 1. Data not seasonally adjusted.
2. Estimates in average prices of previous year.
3. Forecasts in 1998 average prices.

Table A2. Aggregate demand in current prices, 1994–2001 (billion zloty)

		GDP	Domestic demand	Consumption			Investment	Stock-building	Net exports
				total	households	public			
1994	1Q-4Q	223.90	219.07	179.40	139.94	39.46	40.39	-0.71	4.83
1995	1Q-4Q	306.32	299.08	238.38	184.78	53.60	57.40	3.30	7.24
1996	1Q-4Q	385.45	391.48	306.66	239.76	66.90	80.39	4.43	-6.03
1997	1Q-4Q	469.37	489.75	373.74	293.87	79.88	110.85	5.15	-20.37
1998	1Q-4Q	549.47	578.47	433.47	342.88	90.58	139.20	5.80	-29.01
1999e1	1Q-4Q	611.58	655.92	487.45	386.39	101.06	162.10	6.37	-44.34
forecast									
2000	*1Q-4Q*	*698.98*	*749.81*	*551.30*	*438.53*	*112.76*	*192.08*	*6.44*	*-50.83*
2001	*1Q-4Q*	*786.35*	*846.01*	*609.85*	*487.62*	*122.24*	*229.26*	*6.90*	*-59.66*
1995	1Q	69.22	66.24	54.61	42.48	12.12	10.66	0.98	2.98
	2Q	73.85	72.23	59.13	45.23	13.90	12.16	0.94	1.62
	3Q	78.92	76.34	61.01	47.53	13.48	14.49	0.85	2.58
	4Q	84.33	84.27	63.63	49.53	14.10	20.09	0.54	0.06
1996	1Q	84.72	83.37	71.77	55.99	15.78	10.97	0.63	1.35
	2Q	92.28	93.79	77.11	59.87	17.24	15.95	0.72	-1.51
	3Q	97.87	100.20	78.24	61.27	16.97	20.93	1.03	-2.33
	4Q	110.58	114.13	79.53	62.63	16.91	32.54	2.05	-3.54
1997	1Q	103.08	104.93	88.53	69.53	19.00	15.48	0.92	-1.85
	2Q	112.24	116.84	92.52	73.12	19.40	23.29	1.03	-4.60
	3Q	118.39	123.01	94.93	75.50	19.43	27.13	0.96	-4.62
	4Q	135.66	144.96	97.76	75.72	22.05	44.96	2.24	-9.30
1998	1Q	122.69	128.89	106.21	84.25	21.96	21.54	1.14	-6.20
	2Q	132.36	138.72	108.04	84.56	23.48	29.37	1.31	-6.36
	3Q	138.97	145.91	111.28	87.94	23.33	33.30	1.33	-6.94
	4Q	155.45	164.95	107.94	86.13	21.80	54.99	2.02	-9.50
1999e1	1Q	133.58	143.79	119.03	94.07	24.96	24.67	0.09	-10.21
	2Q	146.03	158.37	122.79	96.38	26.42	34.19	1.39	-12.34
	3Q	154.35	164.05	122.95	97.52	25.43	38.89	2.21	-9.70
	4Q	177.62	189.71	122.67	98.42	24.25	64.36	2.68	-12.09
2000	1Qe2	155.53	168.90	135.93	108.05	27.88	31.28	1.69	-13.37
forecast									
2000	*2Q*	*167.71*	*182.73*	*140.12*	*110.35*	*29.77*	*41.10*	*1.51*	*-15.02*
	3Q	*175.20*	*185.48*	*138.86*	*110.52*	*28.34*	*45.26*	*1.35*	*-10.27*
	4Q	*200.53*	*212.70*	*136.38*	*109.61*	*26.77*	*74.44*	*1.88*	*-12.17*
2001	*1Q*	*175.65*	*190.27*	*151.03*	*120.60*	*30.43*	*37.44*	*1.80*	*-14.61*
	2Q	*189.52*	*206.70*	*155.43*	*122.94*	*32.49*	*49.67*	*1.60*	*-17.19*
	3Q	*196.48*	*209.09*	*153.54*	*122.90*	*30.64*	*53.85*	*1.70*	*-12.61*
	4Q	*224.70*	*239.95*	*149.86*	*121.19*	*28.67*	*88.29*	*1.80*	*-15.25*

Source: Data and estimates (e1) – CSO; estimates (e2) and forecast – CASE.

Note: Domestic demand is defined as the sum of consumption of households, public consumption, non-commercial institutions' consumption and investment. Consumption of non-commercial institutions is not separated in the table.

Table A3. Aggregate demand in 1998 prices, 1994–2001 (% change yoy)

		GDP	Domestic demand	Consumption			Investment	Exports	Imports
				total	households	public			
1994	1Q-4Q	5.2	4.8	3.9	4.3	2.8	9.2	13.1	11.3
1995	1Q-4Q	7.0	5.5	3.2	3.3	2.9	16.5	22.8	24.3
1996	1Q-4Q	6.0	9.7	7.2	8.3	3.4	19.7	12.0	28.0
1997	1Q-4Q	6.9	9.3	6.1	6.9	3.4	21.7	12.2	21.4
1998	1Q-4Q	4.8	6.4	4.1	4.7	1.8	14.2	14.3	18.5
1999e1	1Q-4Q	4.1	4.9	4.2	5.0	1.4	6.9	-1.5	1.9
forecast									
2000	*1Q-4Q*	*5.4*	*5.2*	*3.4*	*3.9*	*1.7*	*10.9*	*5.4*	*4.8*
2001	*1Q-4Q*	*6.3*	*6.8*	*4.3*	*4.9*	*2.0*	*13.7*	*8.6*	*9.8*
1996	1Q	3.4	8.0	7.1	8.1	3.4	13.1	14.0	29.7
	2Q	5.5	6.8	3.4	6.1	-5.3	20.5	9.3	28.2
	3Q	7.2	10.6	6.7	7.9	2.6	26.8	12.4	32.4
	4Q	7.9	13.1	11.6	11.1	13.6	17.3	12.2	23.1
1997	1Q	6.9	7.9	6.0	6.7	3.5	19.6	11.3	23.8
	2Q	7.5	9.1	6.4	7.1	3.7	21.0	13.7	22.9
	3Q	6.7	9.4	6.3	7.0	3.6	21.2	6.7	19.0
	4Q	6.4	10.5	5.7	6.6	2.6	23.2	17.3	20.3
1998	1Q	6.5	7.2	5.4	6.2	2.4	17.3	26.6	34.5
	2Q	5.3	5.7	3.5	3.9	1.7	14.6	18.1	23.4
	3Q	4.9	6.1	3.8	4.3	1.6	14.2	14.7	17.2
	4Q	2.9	6.6	3.9	4.5	1.3	12.9	0.2	3.3
1999e1	1Q	1.6	3.3	3.7	4.3	1.4	6.1	-8.9	-2.8
	2Q	3.0	4.6	4.1	4.9	1.3	6.8	-3.5	2.4
	3Q	5.0	5.6	4.5	5.3	1.5	7.0	3.1	5.4
	4Q	6.2	5.8	4.6	5.4	1.4	7.3	3.8	2.7
2000	1Qe2	6.0	6.6	4.2	4.8	2.0	11.7	4.9	6.7
forecast									
2000	*2Q*	*5.0*	*5.3*	*3.5*	*3.9*	*2.0*	*11.9*	*4.2*	*5.4*
	3Q	*4.9*	*4.3*	*3.1*	*3.5*	*1.3*	*10.8*	*6.1*	*3.9*
	4Q	*5.7*	*4.9*	*3.0*	*3.4*	*1.3*	*10.0*	*6.4*	*3.3*
2001	*1Q*	*5.9*	*5.9*	*4.2*	*4.8*	*2.0*	*13.5*	*9.8*	*9.0*
	2Q	*6.6*	*6.9*	*4.5*	*5.1*	*2.0*	*15.2*	*9.0*	*9.5*
	3Q	*6.1*	*6.8*	*4.4*	*5.0*	*2.0*	*13.2*	*8.0*	*10.0*
	4Q	*6.5*	*7.4*	*4.2*	*4.7*	*2.0*	*13.3*	*7.7*	*10.6*

Source: Data and estimates (e1) – CSO; estimates (e2) and forecasts – CASE.

Notes: 1. Domestic demand is defined as the sum of households' consumption, non-commercial institutions' consumption, public consumption and investment. Consumption of non-commercial institutions is not separated in the table.

2. Data are not seasonally adjusted.

3. Estimates in average prices of previous year.

Table A4. Employment, 1994–2001 ('000)

		Total	Paid employment				Market services	Non-market services
			of which employment	agriculture and forestry	manufacturing, mining, etc.	construction		
1994	1Q-4Q	14475	8519	3887	3641	820	3938	2189
1995	1Q-4Q	14735	8570	3836	3757	841	4054	2248
1996	1Q-4Q	15021	8548	4010	3730	843	4161	2277
1997	1Q-4Q	15439	8637	3985	3740	908	4489	2316
1998	1Q-4Q	15800	8752	3969	3701	961	4798	2371
1999	1Q-4Q	15658	8702	3931	3529	954	4840	2404
forecast								
2000	*1Q-4Q*	*15556*	*8575*	*3905*	*3340*	*953*	*4934*	*2425*
2001	*1Q-4Q*	*15756*	*8515*	*3895*	*3363*	*990*	*5039*	*2470*
1994	1Q	14300	8486	3891	3634	797	3833	2145
	2Q	14431	8485	3895	3629	822	3933	2152
	3Q	14461	8517	3916	3630	829	3927	2159
	4Q	14706	8587	3904	3667	831	4004	2300
1995	1Q	14489	8507	3839	3739	800	3878	2233
	2Q	14711	8562	3835	3757	847	4039	2233
	3Q	14763	8534	3863	3752	855	4074	2219
	4Q	14977	8668	3856	3780	862	4172	2307
1996	1Q	14682	8487	4002	3714	737	3969	2260
	2Q	14932	8513	4001	3719	837	4120	2255
	3Q	15083	8522	4044	3730	879	4181	2249
	4Q	15386	8671	4038	3759	919	4326	2344
1997	1Q	15048	8567	3982	3753	788	4235	2290
	2Q	15374	8645	3980	3733	910	4441	2311
	3Q	15594	8675	4020	3735	952	4578	2309
	4Q	15739	8706	4006	3740	981	4656	2356
1998	1Q	15506	8717	3956	3717	864	4609	2360
	2Q	15819	8759	3953	3722	978	4804	2362
	3Q	15921	8714	3991	3676	1010	4901	2343
	4Q	15953	8817	3976	3688	992	4879	2418
1999	1Q	15423	8747	3900	3587	871	4635	2430
	2Q	15680	8717	3925	3543	973	4831	2408
	3Q	15748	8649	3960	3507	1001	4914	2366
	4Q	15782	8695	3940	3480	970	4982	2410
2000	1Q	15185	8590	3880	3350	840	4705	2410
forecast								
2000	*2Q*	*15518*	*8570*	*3890*	*3330*	*970*	*4918*	*2410*
	3Q	*15678*	*8540*	*3920*	*3330*	*1000*	*5018*	*2410*
	4Q	*15845*	*8600*	*3930*	*3350*	*1000*	*5095*	*2470*
2001	*1Q*	*15405*	*8510*	*3880*	*3350*	*880*	*4825*	*2470*
	2Q	*15678*	*8500*	*3880*	*3350*	*1000*	*5008*	*2440*
	3Q	*15888*	*8490*	*3910*	*3370*	*1040*	*5118*	*2450*
	4Q	*16055*	*8560*	*3910*	*3380*	*1040*	*5205*	*2520*

Source: Annual data – CSO; quarterly data and forecasts – CASE.
Note: Employment is calculated according to the CSO's methodology.

Table A5. Unemployment, 1995–2001

		Registered unemployment		Unemployment LFS	
		(' 000)	%	(' 000)	%
1995	1Q-4Q	2629	14.9	2233	13.1
1996	1Q-4Q	2360	13.2	1961	11.5
1997	1Q-4Q	1826	10.3	1737	10.2
1998	1Q-4Q	1831	10.4	1827	10.6
1999	1Q-4Q	2350	13.0		
forecast					
2000	*1Q-4Q*	2447	13.4		
2001	*1Q-4Q*	2397	13.1		
1995	1Q	2754	15.5	2491	14.7
	2Q	2694	15.2	2156	12.6
	3Q	2657	15.0	2227	12.9
	4Q	2629	14.9	2233	13.1
1996	1Q	2726	15.4	2349	14
	2Q	2508	14.3	2103	12.4
	3Q	2341	13.5	2018	11.6
	4Q	2360	13.2	1961	11.5
1997	1Q	2236	12.6	2176	12.8
	2Q	2040	11.6	1927	11.3
	3Q	1854	10.7	1853	10.7
	4Q	1826	10.3	1737	10.2
1998	1Q	1846	10.4	1896	11.1
	2Q	1688	9.6	1753	10.2
	3Q	1677	9.6	1786	10.3
	4Q	1831	10.4	1827	10.6
1999	1Q	2170	12.1	2141	12.5
	2Q	2074	11.6		
	3Q	2178	12.1		
	4Q	2350	13.0		
2000	1Q	2509	13.9		
forecast					
2000	*2Q*	*2397*	*13.3*		
	3Q	*2408*	*13.3*		
	4Q	*2447*	*13.4*		
2001	*1Q*	*2449*	*13.5*		
	2Q	*2397*	*13.2*		
	3Q	*2358*	*12.9*		
	4Q	*2397*	*13.1*		

Source: Data – CSO; LSF estimates for 2Q99 and 3Q99, and forecasts – CASE.
Note: The CSO stopped publishing LFS (labour force survey) statistics in 2Q99.

Table A6. Selected price indices, 1997–2000 (% yoy)

		CPI	PPI		Export price index	Import price index
			Manufacturing, etc.	Construction		
1997	01	17.8	12.9	14.5	12.5	16.0
	02	17.3	11.9	14.4	7.9	13.4
	03	16.6	11.8	14.5	12.7	9.8
	04	15.3	12.0	14.5	11.9	11.6
	05	14.6	12.4	14.4	9.2	17.0
	06	15.3	12.2	14.0	14.1	8.6
	07	14.9	12.0	14.3	14.5	14.1
	08	14.5	12.5	14.2	10.5	16.2
	09	13.6	13.0	14.1	15.2	14.7
	10	13.1	12.1	14.3	16.3	13.1
	11	13.2	12.1	14.2	12.9	14.8
	12	13.2	11.5	14.5	13.4	14.5
1998	01	13.6	9.2	15.7	9.8	7.9
	02	14.2	9.1	15.7	10.0	11.0
	03	13.9	9.2	15.4	11.5	10.4
	04	13.7	8.4	14.6	8.4	4.4
	05	13.3	8.2	14.4	8.2	0.7
	06	12.2	7.7	14.1	7.8	4.4
	07	11.9	7.0	13.6	6.9	1.5
	08	11.3	6.6	13.0	4.4	- 5.6
	09	10.6	6.4	12.4	7.0	3.3
	10	9.9	5.8	11.7	3.8	3.4
	11	9.2	5.1	11.1	3.2	- 2.3
	12	8.6	4.8	10.6	4.7	- 5.1
1999	01	6.9	3.9	9.9	2.8	-0.3
	02	5.6	3.7	9.4	9.6	1.5
	03	6.2	4.7	9.0	10.7	5.6
	04	6.3	5.0	8.6	9.9	9.0
	05	6.4	5.2	8.4	10.2	8.2
	06	6.5	5.2	8.1	1.1	4.8
	07	6.3	5.5	7.8	0.3	5.2
	08	7.2	5.9	7.8	7.2	10.3
	09	8.0	6.2	8.2	6.3	4.6
	10	8.7	6.8	8.3	11.0	7.4
	11	9.2	7.5	8.6	13.5	11.7
	12	9.8	8.1	8.9	10.8	15.1
2000	01	10.1	8.2	7.7		
	02	10.4	8.1	7.5		
	03	10.3	7.4	7.6		

Source: CSO.

Table A7. Exchange rates, 1997–2000 (in zloty)

		US$/zloty	DM/zloty	euro(ECU)/zloty
1997	01	2.9273	1.8312	3.5538
	02	3.0279	1.8104	3.5132
	03	3.0793	1.8163	3.5276
	04	3.1212	1.8250	3.5604
	05	3.1713	1.8605	3.6272
	06	3.2385	1.8749	3.6618
	07	3.3965	1.8962	3.7416
	08	3.4817	1.8948	3.7276
	09	3.4566	1.9333	3.7917
	10	3.4223	1.9454	3.8226
	11	3.5033	2.0230	3.9996
	12	3.5256	1.9852	3.9268
1998	01	3.5316	1.9461	3.8432
	02	3.5386	1.9505	3.8503
	03	3.4593	1.8941	3.7560
	04	3.4194	1.8827	3.7329
	05	3.4188	1.9246	3.7917
	06	3.4789	1.9420	3.8362
	07	3.4592	1.9226	3.8002
	08	3.5850	2.0046	3.9543
	09	3.6066	2.1211	4.1713
	10	3.4955	2.1353	4.2071
	11	3.4496	2.0514	4.0323
	12	3.4858	2.0884	4.0979
1999	01	3.5417	2.1007	4.1087
	02	3.7948	2.1727	4.2494
	03	3.9430	2.1927	4.2886
	04	4.0016	2.1905	4.2843
	05	3.9368	2.1387	4.1830
	06	3.9431	2.0947	4.0969
	07	3.8827	2.0537	4.0166
	08	3.9510	2.1447	4.1946
	09	4.0799	2.1925	4.2881
	10	4.1092	2.2513	4.4031
	11	4.2527	2.2484	4.3974
	12	4.1696	2.1577	4.2200
2000	01	4.1036	2.1274	4.1608
	02	4.1439	2.0886	4.0850
	03	4.0902	2.0200	3.9507

Source: NBP.
Notes: 1. Monthly average.
2. Until end-1998 the Ecu exchange rate, then the euro exchange rate.

Table A8. Foreign trade, 1997–2000 (US$ million)

		Exports		Imports		Net exports	
		CSO	NBP	CSO	NBP	CSO	NBP
1997	01	2011	1905	3405	3383	- 1394	- 1478
	02	2029	1941	3051	2650	- 1022	- 709
	03	2081	1920	3313	2805	- 1231	- 885
	04	2180	2361	3652	3319	- 1472	- 958
	05	1947	2035	3336	2864	- 1388	- 829
	06	2187	2296	3569	3196	- 1382	- 900
	07	2015	2372	3396	3275	- 1382	- 903
	08	1888	2157	3073	2876	- 1186	- 719
	09	2304	2489	3677	3397	- 1373	- 908
	10	2676	2790	3999	3654	- 1324	- 864
	11	2292	2359	3898	3311	- 1606	- 952
	12	2142	2604	3940	3819	- 1797	- 1215
1998	01	2156	2120	3172	3565	-1016	-1445
	02	2377	2265	3667	3078	-1290	-813
	03	2490	2671	4248	3657	-1758	-986
	04	2340	2468	3849	3496	-1509	-1028
	05	2300	2449	3886	3350	-1586	-901
	06	2401	2753	3959	3699	-1558	-946
	07	2393	2936	3929	3924	-1537	-988
	08	2168	2529	3552	3309	-1385	-780
	09	2332	2336	4516	3864	-2183	-1528
	10	2621	2533	4372	3908	-1750	-1375
	11	2369	2369	4098	3695	-1728	-1326
	12	2283	2693	3807	4297	-1524	-1604
1999	01	2027	2119	3147	3331	-1120	-1212
	02	2092	2495	3239	3279	-1147	-784
	03	2452	2398	4034	3223	-1583	-825
	04	2167	2159	3633	3195	-1466	-1036
	05	2237	1989	3700	3020	-1463	-1031
	06	2154	2122	3667	3424	-1514	-1302
	07	2119	2092	3761	3414	-1641	-1322
	08	2193	2078	3651	3308	-1458	-1230
	09	2438	2044	4093	3353	-1655	-1309
	10	2595	2221	4324	3360	-1729	-1139
	11	2511	2151	4373	3712	-1862	-1561
	12	2423	2470	4290	4235	-1866	-1765
2000	01	2236	1922	3488	3380	-1252	-1458
	02	2118	2072	3700	3191	-1582	-1119
	03		2341		3596		-1255

Source: NBP and CSO.
Notes: 1. NBP data on payments basis, CSO's data on SAD basis.
2. NBP data for February and March – preliminary.

Table A9. Balance of payments, 1997–2000 (US$ million)

		Balance on						Gross foreign exchange reserves
		current account	merchandise trade	current transfers	unclassified current transactions	direct investment	portfolio investment	
1997	01	-898	-1478	87	379	108	204	-559
	02	-228	-709	89	350	138	352	-306
	03	-408	-885	80	391	210	-148	374
	04	-766	-958	111	493	317	528	-668
	05	-139	-829	88	524	168	310	-328
	06	-289	-900	78	454	294	233	-954
	07	-318	-903	103	508	290	301	-44
	08	-138	-719	68	527	110	203	-419
	09	-454	-908	90	589	377	135	1
	10	-64	-864	120	762	477	421	-823
	11	-283	-952	96	509	292	-246	-8
	12	-327	-1215	140	525	260	-195	143
1998	01	-963	-1443	102	374	477	-309	-97
	02	-278	-813	131	397	150	268	-2197
	03	-755	-986	120	392	277	253	-284
	04	-428	-1001	121	578	334	89	-848
	05	-200	-901	117	587	539	130	-492
	06	-8	-945	399	550	248	144	-650
	07	-102	-988	192	574	589	121	-1378
	08	183	-780	165	856	661	-643	-174
	09	-1296	-1528	163	438	496	-336	649
	10	-962	-1375	159	449	359	-73	228
	11	-830	-1326	149	363	201	723	-634
	12	-1187	-1604	124	437	638	963	178
1999	01	-894	-1212	101	320	291	-81	74
	02	-512	-784	102	242	317	-177	-83
	03	-833	-825	176	237	530	-46	-142
	04	-938	-1036	113	232	364	2	108
	05	-690	-1031	108	300	403	-251	64
	06	-1134	-1302	132	253	382	167	0
	07	-1055	-1322	138	301	297	70	-47
	08	-783	-1230	142	429	1393	228	-26
	09	-1147	-1309	137	423	788	-388	442
	10	-849	-1139	130	426	363	451	76
	11	-1178	-1561	148	299	789	809	-116
	12	-1640	-1706	161	174	681	306	-120
2000	01	-1207	-1458	113	286	763	298	-407
	02	-954	-1140	113	225	354	587	-59
	03	-1431	-1240	133	218	400	1619	-42

Source: NBP.
Note: February and March data – preliminary.

Table A10. Interest rates, 1997–2001

		Rediscount rate	Lombard rate	3-month WIBOR	28-day repo rate
1997	01	22.0	25.0	22.4	-
	02	22.0	25.0	22.5	-
	03	22.0	25.0	22.6	-
	04	22.0	25.0	22.8	-
	05	22.0	25.0	22.8	-
	06	22.0	25.0	22.7	-
	07	22.0	25.0	24.0	-
	08	24.5	27.0	25.6	-
	09	24.5	27.0	25.4	-
	10	24.5	27.0	25.2	-
	11	24.5	27.0	25.3	-
	12	24.5	27.0	25.7	-
1998	01	24.5	27.0	26.1	23.5
	02	24.5	27.0	25.2	24.0
	03	24.5	27.0	25.1	23.0
	04	24.5	27.0	24.5	23.0
	05	23.5	26.0	23.2	21.5
	06	23.5	26.0	22.1	21.5
	07	21.5	24.0	21.0	19.0
	08	21.5	24.0	19.8	19.0
	09	21.5	24.0	18.8	18.0
	10	20.0	22.0	17.9	17.0
	11	20.0	22.0	16.7	17.0
	12	18.3	20.0	15.9	15.5
1999	01	15.5	17.0	14.8	13.0
	02	15.5	17.0	13.2	13.0
	03	15.5	17.0	13.2	13.0
	04	15.5	17.0	13.2	13.0
	05	15.5	17.0	13.3	13.0
	06	15.5	17.0	13.3	13.0
	07	15.5	17.0	13.4	13.0
	08	15.5	17.0	13.7	13.0
	09	15.5	17.0	14.3	14.0
	10	15.5	17.0	16.6	14.0
	11	19.0	20.5	18.2	16.5
	12	19.0	20.5	18.0	16.5
2000	01	19.0	20.5	17.2	16.5
	02	20.0	21.5	17.8	17.5
	03	20.0	21.5	18.4	17.5
forecast					
	2Q00	-	*21.5*	*17.89*	-
	2000	-	*18.5*	*16.35*	-
	2001	-	*15.5*	*12.66*	-

Source: Data – NBP and forecasts – CASE.
Notes: 1. End-month except for WIBOR – monthly average.
2. End-period forecast.

Table A11. Monetary indicators, 1997–2001 (billion zloty)

		M0	M2	Cash	Zloty deposits			Foreign currency deposits	Credits			Net liabilities of the budgetary sector
					total	individual	corporate		total	individual	corporate	
1997	1Q-4Q	42.3	176.4	27.3	118.3	80.9	37.4	30.8	108.3	18.4	89.9	55.3
1998	1Q-4Q	53.6	220.8	30.2	156.9	109.6	47.3	33.6	138.5	23.9	114.6	61.3
1999	1Q-4Q	47.9	263.5	38.1	185.7	124.1	61.6	39.7	175.9	36.6	139.3	64.5
forecast												
2000	*1Q-4Q*	*52.1*	*305.5*	*34.0*	*226.0*	*159.0*	*67.0*	*45.5*	*211.4*	*45.0*	*166.4*	*63.8*
2001	*1Q-4Q*	*61.7*	*362.0*	*35.0*	*277.0*	*199.0*	*78.0*	*50.0*	*253.4*	*57.0*	*196.4*	*67.0*
1997	1Q	37.7	141.6	24.6	91.9	63.3	28.7	25.0	88.0	12.8	75.2	49.9
	2Q	41.2	151.8	26.8	98.5	68.5	30.0	26.5	94.5	14.8	79.7	49.8
	3Q	44.1	162.3	27.6	105.9	73.3	32.6	28.7	102.2	16.4	85.8	49.1
	4Q	42.3	176.4	27.3	118.3	80.9	37.4	30.8	108.3	18.4	89.9	55.3
1998	1Q	44.4	180.4	27.3	123.3	88.9	34.4	29.8	114.7	18.6	96.1	50.3
	2Q	49.7	192.3	29.7	132.9	95.1	37.8	29.7	122.1	20.1	102.0	50.7
	3Q	49.7	203.5	30.3	142.3	101.8	40.5	30.9	131.0	21.9	109.0	56.8
	4Q	53.6	220.8	30.2	156.9	109.6	47.3	33.6	138.5	23.9	114.6	61.3
1999	1Q	53.9	230.3	32.0	161.2	116.5	44.6	37.1	148.6	25.3	123.3	63.9
	2Q	59.1	236.2	33.6	166.2	119.2	47.0	36.4	155.8	28.3	127.5	65.2
	3Q	46.2	246.0	34.2	173.3	122.4	51.0	38.5	167.4	32.4	135.0	61.6
	4Q	47.9	263.5	38.1	185.7	124.1	61.6	39.7	175.9	36.6	139.3	64.5
2000	1Q	48.0	261.7	33.0	186.2	134.3	51.9	42.6	183.8	38.3	145.4	60.0
forecast												
2000	*2Q*	*49.0*	*274.3*	*34.0*	*196.0*	*141.0*	*55.0*	*44.3*	*189.8*	*39.4*	*150.4*	*61.0*
	3Q	*49.7*	*287.4*	*34.4*	*207.5*	*147.5*	*60.0*	*45.5*	*201.6*	*41.5*	*160.1*	*61.3*
	4Q	*52.1*	*305.5*	*34.0*	*226.0*	*159.0*	*67.0*	*45.5*	*211.4*	*45.0*	*166.4*	*63.8*
2001	*1Q*	*57.2*	*312.0*	*35.0*	*231.5*	*168.5*	*63.0*	*45.5*	*224.2*	*48.5*	*175.7*	*61.9*
	2Q	*58.2*	*326.0*	*35.0*	*244.0*	*178.0*	*66.0*	*47.0*	*231.0*	*51.0*	*180.0*	*62.8*
	3Q	*59.0*	*341.3*	*35.3*	*258.0*	*188.0*	*70.0*	*48.0*	*244.1*	*53.5*	*190.6*	*64.3*
	4Q	*61.7*	*362.0*	*35.0*	*277.0*	*199.0*	*78.0*	*50.0*	*253.4*	*57.0*	*196.4*	*67.0*

Source: Data – NBP and forecasts – CASE.